[Key issues when acting for a borrower during a pandemic or crisis]

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Introduction to acting for a borrower during a pandemic or crisis

During a pandemic or crisis, economic uncertainty and market volatility will concern borrowers. When acting for a borrower, it is prudent to help ensure their financing arrangements can proceed or be preserved as much as possible, including by having sensible dialogue with their lender as early as possible.

Lenders would often prefer to hold off on calling defaults if possible to avoid adverse publicity, such as being labelled as not supporting borrowers in hard times. In practice, this means more often than not, a lender would be open to negotiating a mutually beneficial variation to the terms of the original loan agreement so the transaction can survive. Any such discussion with the lender should be entered into in a timely manner, such as ahead of tripping a covenant.

With these things in mind, this guidance note discusses some key issues for consideration when acting for a borrower during a pandemic or crisis. When advising on matters relating to financing during a pandemic or crisis, legal practitioners should also consider issues relating to triggering default provisions, providing repeating representations, among others. See *Financing during a pandemic or crisis*.

Considerations relating to the availability of credit

During a pandemic or crisis, borrowers should consider their existing finance arrangements, and assess matters such as:

- levels of credit already drawn; and
- credit available for drawing.

The outcome of the assessment can guide the way forward. For example:

- Undraw commitments — If a borrower has undrawn commitments, it could request a drawdown on those undraw commitments to bolster its financial position to survive the challenges pose by the pandemic or crisis.
- Lines of credit — A borrower could also consider obtaining greater lines of credit, such as overdraft accounts or working capital facilities (see *Overdrafts, term loans and revolving credit facilities*). This may suit a borrower who does not already have substantial financing on foot.
- Alternative sources of capital — If a borrower is not able to obtain lines of credit from the lender (due to not meeting the lender's requirements or the lender does not have any funds to provide), the borrowers could seek alternative sources of capital, including parent company loans or further injection of equity by shareholders.

Considerations relating to negotiating more manageable terms

Preparing to negotiate

During a pandemic or crisis, borrowers who wish to negotiate with their lenders to seek more manageable terms need to, among other things:

- be ready to discuss their economic resilience; and
- be able to demonstrate how any effects are contained or are otherwise managed.

What to negotiate

An approach or strategy that suits one borrower may not suit another, but generally, a borrower could seek to amend the finance documents for leniency with regards to meeting payment obligations. This is because during a pandemic or crisis, as borrower's experience business disruption which impacts on cash flow, perhaps the most obvious default would be those relating to non-payment. A failure to make repayment (of principle and/or interest) by its due date will in most cases be an immediate event of default. See *Repayment, prepayment and cancellation* and *Events of default when acting for the borrower*.

Against this background, a borrower may wish to ask for:

- shorter interest periods;
- repricing; and/or
- extensions of maturity date.

Practice Tip: A borrower who requests for an extension of maturity date should be aware of the consequences, such as:

- balloon payments being delayed for bullet loans; or
- decreasing instalment payments for amortising loans (see *Repayment, prepayment and cancellation*).

This is also coupled with the trade-off of increased interest payments over the long run.

A borrower may also wish to seek waivers for other potential of actual defaults, such as a breach of a financial covenant. See *Financial covenants — principles*.

What to expect

Borrowers need to mindful that where leniency is sought in the form of amendment or waivers to the terms, they can expect lenders to seek quid pro quo (something for something). This may be in the form of:

- additional guarantees (see *Overview — Types of guarantees and indemnities in financing transactions*);
- additional securities (see *Mortgage of land — the essentials*, *Overview — Non-mortgage securities* and *Security agreements — the essentials*);
- increase reporting obligations,
- consent fees;
- variation fees; and
- repricing.

Government assistance and legislative relief

While borrowers could look to lenders for assistance during a pandemic or crisis, borrowers could also look to the Government for help as it releases stimulus packages and support programs. For example, in response to the domestic and global challenges brought about by the COVID-19 pandemic, initiatives are developed by Federal, State and Territory Governments to help businesses maintain cash flow, support trade and commerce, and address certain industry or sector specific issues. For example:

- eligible loans to small and medium-sized enterprises (SMEs) who must have a turnover of less than $50 million including sole traders and not-for-profit organisations — see *Coronavirus SME Guarantee Scheme* on The *Treasury*'s website;
- funding of up to $25,000 for eligible small to medium food and agrifood businesses affected by natural catastrophe or global disease outbreaks (such as COVID-19 and African Swine Fever) — see Black Summer Innovation Program *factsheet* by Food Innovation Australia (often referred to as "FIAL").

Borrowers should carefully consider the full range of packages and programs available when determining how to best respond to challenges both during and after a pandemic or crisis. Government packages and programs are often rolled out in a progressive manner. Legal practitioners can assist in many ways, including advising on the nature of a benefit and details relating to eligibility.

Borrowers should also be aware other non-credit Government measures that could assist with business continuity. For example, the NSW Government has introduced regulations to temporarily enable legal documents to be witnessed remotely in real time by authorised witnesses via audio visual link (currently till 26 September 2020). The changes have been introduced under *s 17* of the Electronic Transactions Act 1999 (Cth). It is expected that other States would follow NSW's lead. See *Signing documents remotely or electronically in a pandemic or crisis*.
References: *s 17, Electronic Transactions Act 1999 (Cth)*

Addressing solvency concerns

If the revenue impacts of a pandemic or crisis is endangering a borrower's cash-flow solvency, then the 2018 insolvency law reform relating to "safe harbour" measures should be considered, as it may help a borrower trade through the period of concern.

In short, in 2018, changes to *s 588GA* of the Corporations Act 2001 (Cth) (Corporations Act) introduced "safe harbour" provisions for directors of companies. The changes, subject to certain exceptions, allow directors to make efforts to restructure the company outside the formal insolvency process at a time when insolvency is suspected. Further, the Corporations Act was amended to restrict the right of parties to enforce so-called "ipso facto" clauses. Where a party to a contract has entered into insolvency, an ipso facto clause can allow the other party to terminate the contract or exercise other rights, even where the first party continues to perform the contract. These reforms mean that an entity can stay (or suspend) the enforcement of an express contractual right against it under an ipso facto clause where, broadly speaking:
References: *s 588GA, Corporations Act 2001 (Cth)*

- the entity enters (or in some cases, announces that it will enter) into a compromise or arrangement to avoid being wound up in insolvency;
- a managing controller of the whole or substantially the whole of the property of the entity is appointed to that entity; or
- the entity goes into administration.

Practice Tip: The Government has announced temporary changes to some aspects of existing insolvency laws as part of the plan to try and keep businesses operating during the crisis prompted by COVID-19, as set out in the Government's publication "*Temporary relief for financially distressed businesses*", available on *Business* website.

Consumer credit borrowers

"Consumer credit" is a form of credit advanced to a consumer (a natural person) for the purpose of purchasing certain goods or services, such as those wholly or predominantly for personal domestic or household purposes. Examples include credit cards, store cards, personal loans and mortgages. See *What is consumer credit and what credit contracts are regulated by the NCC?*.

The principal legislation governing consumer credit is the *National Consumer Credit Protection Act 2009* (Cth). It provides that a debtor, mortgagor or guarantor may negotiate with a credit provider to vary obligations under a credit contract, mortgage or guarantee at any time. There are two mechanisms whereby a debtor can formally apply to a credit provider and, if unsuccessful, to the court, to vary their obligations under a credit contract — by a hardship notice or a postponement request. See *Hardship and unjust transactions*.

During a pandemic or crisis, a consumer credit borrower may wish to consider these mechanisms and whether they could, or should apply, to the lender for a variation to the terms of the original loan agreement to avoid a breach that could lead to a default. See *Default under consumer credit contracts*.

For further guidance on advising a consumer credit borrower on matters relating to hardship and default during a pandemic or crisis, see *Hardship and default during a pandemic or crisis*.