

What's inside?

UK High Court: chargor's degree of control relevant in characterising a fixed charge.....	1
ARRC Issues Updates to Term SOFR Best Practice Recommendations.....	2
FSB urges market participants to make final preparations for USD LIBOR transition.....	3
Corruption Prevention Guide for Banks.....	3
Regtech Adoption Practice Guide.....	3
HKMA, SFC publish joint consultation on amendments to clearing rules.....	4

UK High Court: chargor's degree of control relevant in characterising a fixed charge

Simon Deane and Ally Leow

The English High Court (“**Court**”) in *Re Avanti Communications Limited (In Administration)* [2023] EWHC 940 (Ch) (“**Re Avanti**”) ruled that the existence of permitted disposals of secured assets under a security document does not necessarily undermine the fixed charge over the said assets.

Background

Avanti Communications (the “**Company**”) had granted fixed charges over certain satellite and network communications assets (“**Relevant Assets**”) as security for several finance documents. The security contained restrictions against disposal, and permissions to dispose, of the Relevant Assets subject to specified conditions.

Issue

The Company and the administrators sought a determination of whether the Relevant Assets which had been sold by the Company were subject to a fixed or floating charge.

The characterisation of the charge would affect the amount recovered by secured creditors. If the charge was found to be floating, a portion of the proceeds would go to HM Revenue & Customs (as preferential creditor), and into the ring-fenced sum held for unsecured creditors. If fixed, the proceeds would be retained by the secured creditors.

Ruling

The Court confirmed the two-stage test approach set out by Lord Millet in *Agnew v Commissioners of Inland Revenue*.¹ At the first stage, the court must construe the relevant instrument of charge to ascertain the nature of the rights and obligations which the parties intended to grant each other over the charged assets. At the second stage, the court must characterise the charge and determine whether the rights and obligations in respect of the charged assets are consistent with fixed charge security or floating charge security; this is a question of law independent of the parties' intentions.

The Court was satisfied from the debentures that the Relevant Assets were within the scope of the charging clause. It further observed that the parties had expressed the charge as a fixed charge, though reiterating that this is not decisive

¹ [2001] 2 AC 710 at [32]

in the characterisation exercise. The Court also endorsed the distinction drawn in former cases² between (a) assets that are part of a company's circulating capital or stock in trade (indicative of a floating charge); and (b) assets which are specific and do not necessarily fluctuate (indicative of a fixed charge). It concluded that the Relevant Assets fell into the latter category. Lastly, the Court examined the nature of the restrictions against and permissions of disposals of the Relevant Assets in the debentures, and found that, notwithstanding the Company's permissions to dispose of the Relevant Assets, such permissions were "strictly limited" and the Company had "no ability to deal with the Relevant Assets in the ordinary course of its business". Thus, the Court held that the charges took effect as fixed charges.

It is worth noting that, when considering the second stage, the Court did not agree with the absolute approach suggested by some academic commentary, which stipulated a total prohibition on all dealings in the asset or its proceeds as a requirement of a fixed charge. Instead, the Court held that prior case law in this area supports a more nuanced approach which depends on a combination of factors. As such, it was neither feasible nor sensible to pinpoint the location "spectrum of possibilities" where a floating charge gives way to a fixed charge, or vice versa.

Conclusion

Re Avanti makes it clear that a fixed charge does not require a total prohibition on a chargor's ability to deal with its charged assets. Where such assets are not part of the company's circulating capital or fluctuating assets, and the chargor's ability to deal as such is effectively limited, the security may be consistent with a fixed charge. Although *Re Avanti* has not yet been followed by the Hong Kong courts, it is likely to act as persuasive authority in future cases where relevant. Lenders should ensure that security documents and any exceptions to a complete prohibition on disposal of charged assets are clearly and carefully drafted to avoid unintentionally creating a floating charge.

To access the full case, please see [here](#).

ARRC Issues Updates to Term SOFR Best Practice Recommendations

Simon Deane and Natalie Chan

On 21 April 2023, the Alternative Reference Rates Committee ("**ARRC**"), a group of private-market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York in 2014 to lead the LIBOR transition in the United States, issued an update ("**Update**") on the Best Practice Recommendations for, among other things, the use of the Secured Overnight Financing Rate ("**SOFR**") and its term rates ("**Term SOFR**"), following the ARRC's formal recommendation to use Term SOFR in July 2021.

The Update provides clarifications to support the use of Term SOFR as a fallback for, among others, legacy LIBOR cash products, and for new business loans and securitizations that hold underlying Term SOFR assets. The ARRC recommends use of overnight SOFR and SOFR averages in new issuances of all other products but NOT Term SOFR.

The ARRC also recommends the use of overnight SOFR and SOFR averages where a party wishes to hedge in the most efficient and transparent manner. It does not support the use of Term SOFR for the majority of derivatives markets. Any use of Term SOFR-SOFR basis swaps should be limited to dealers facing non-dealers, and any use of other Term SOFR derivatives should be specifically limited to non-dealer facing transactions intended to hedge an end user's direct cash product exposure to Term SOFR. The ARRC recommends that use of all Term SOFR derivatives between dealers be strictly avoided. The limitations are intended to avoid use that is not in proportion to, or materially detracts from, the depth of transactions in the underlying derivatives market that are essential to the construction of the Term SOFR rates over time.

For more details on the Update, please see [here](#).

² See, for example, *Re Cimex Tissues Ltd* [1994] BCC 626 at 635; *Re Spectrum* at [138] and [139]

FSB urges market participants to make final preparations for USD LIBOR transition

Simon Deane and Natalie Chan

The Financial Stability Board (“**FSB**”), an organisation affiliated to the Bank for International Settlements that coordinates the development of effective regulatory, supervisory and other financial sector policies at an international level, issued a press release on 27 April 2023 to push forward final preparations for the USD LIBOR transition.

The panel bank submissions for overnight, 1-month, 3-month, 6-month and 12-month USD LIBOR settings will cease by the end of June 2023. While the FSB notes that substantial efforts have been made in the market to transition away from USD LIBOR, it continues to stress the importance of completing the transition of any remaining USD LIBOR-linked products now, to avoid “pile ups” towards the end of June 2023 that could introduce operational risks and wider market disruption.

To help address outstanding legacy contracts that may require a short period of extra time to complete the transition, the UK Financial Conduct Authority (“**FCA**”) has announced that it will require continued publication of the 1-month, 3-month and 6-month USD LIBOR settings after the end of June 2023 by using a robust, unrepresentative synthetic methodology based on the CME Term SOFR Reference Rate and the ISDA fixed spread adjustment. The publication of these synthetic USD LIBOR settings will cease on 30 September 2024.

Please click [here](#) for more information on the press release.

Corruption Prevention Guide for Banks

Simon Deane and Sally Lau

On 14 March 2023, the Hong Kong Monetary Authority (“**HKMA**”) issued a circular (“**Circular**”) in relation to the Corruption Prevention Guide for Banks (“**Guide**”) published by Hong Kong’s Independent Commission Against Corruption (“**ICAC**”). The Guide was published with the support of the HKMA and the banking industry.

The ICAC developed the Guide to assist Authorized Institutions (“**AIs**”) in the establishment and strengthening of their corruption prevention capabilities. The Guide also includes recommended measures to be adopted by different institutions in the industry. AIs may adopt these measures to suit their operational needs while adhering to the principles.

The HKMA believes that this Guide is a useful tool for AIs to enhance their management personnel’s awareness, knowledge and competence in corruption prevention. By providing a variety of case studies, the Guide helps raise business, compliance and audit managers’ awareness of corruption risk exposures, malpractices and red flags faced by the AIs. The HKMA further recommends practicable mitigation actions and safeguards to help AIs develop a more comprehensive corruption prevention system.

The HKMA strongly recommends adoption of the Guide’s principles by all AIs operating in Hong Kong, by practitioners in the banking industry, and by anyone with an interest in promoting probity standards and ensuring business integrity.

For more information on the Circular, please see [here](#). To access a full copy of the Guide, please see [here](#).

Regtech Adoption Practice Guide

Simon Deane and Chris Wong

On 10 May 2023, the HKMA released its ninth “Regtech Adoption Practice Guide”. The focus of this issue is on “regtech” solutions for banks in relation to the handling and use of customer data and privacy.

As noted in the guide, many banks pointed to customer data and privacy as an area where regtech could be used to ensure that compliance with relevant requirements. The guide provides examples of the challenges faced by banks in Hong Kong regarding customer data and privacy compliance, including divergence of regulatory requirements across jurisdictions and the decentralised and fragmented nature of customer data, as well as potential ways in which regtech can assist with these challenges, including solutions for identifying the data being collected and processed and centralising such data, consent management, data breach responses, etc.

The HKMA offered guidance on the implementation of such solutions, including the need to have and obtain the right operating model and team to handle such solutions, conducting appropriate training, the ability to identify the relevant data being collected and processed, and conducting appropriate risk assessments in relation to privacy.

The regtech guide, the ninth in the series, is a continuation of the HKMA's aim to encourage the adoption of technology by banks as a way to improve on their business and their service to customers, as well as to improve efficiency for the bank and customers alike.

The Regtech Adoption Practice Guide can be found [here](#).

HKMA, SFC publish joint consultation on amendments to clearing rules

Simon Deane and Crystal Choi

On 10 March 2023, the HKMA and the Securities and Futures Commission (“**SFC**”) published a joint consultation paper on the proposed amendments to the mandatory clearing regime, as set out in the Securities and Futures (OTC Derivative Transactions – Clearing and Record Keeping Obligations and Designation of Central Counterparties) Rules.

The proposed changes align with the global interest rate benchmark reform, in particular the transition from the use of interbank offered rates (“**IBORs**”) to alternative reference rates (“**ARRs**”). It is proposed that the current requirement under the Clearing Rules to clear certain OTC derivative transactions referencing IBORs that are no longer or will no longer be published or considered representative should be replaced by the new requirement to clear certain OTC transactions referencing the relevant ARR.

The joint consultation paper is available [here](#).

Want to know more?

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