The impact of COVID-19 on your funding arrangements

Accessing funding during COVID-19

As the extent of the economic impacts of COVID-19 continues to materialise, access to funding will be front of mind for many businesses. Over the past week, the Government, the Reserve Bank and retail banks have announced a number of measures to provide liquidity and generally support the economy affected by the economic impacts of COVID-19.

On 1 April 2020, the Government launched its Business Finance Guarantee scheme for small to medium sized businesses. The scheme allows for banks to make loans of up to $500,000 to businesses with annual turnovers of $250,000 to $80 million for a maximum of three years, with the Government assuming 80% of the credit risk. These loans are expected to be offered on transparent terms, and at competitive market rates.

For businesses with undrawn existing credit facilities, now may be a time to consider whether those facilities can be used for general working capital to cover operating expenses at this time.

Maintaining existing funding

Businesses with existing credit facilities need to be taking stock of your obligations to your financier(s). Downturns in revenue or a suspension of business (all or in part) may give rise to a number of issues in connection with your funding arrangements. Set out below are some practical matters for borrowers to consider and, if necessary, discuss with your financier(s). Please note that the examples noted below are general in nature, and the wording of any specific provisions and their impact will need to be considered on a case-by-case basis.

- **Events of default**: Borrowers should review their finance documents to refresh themselves as to any events of default (and review events) in their loan facilities. A number of these could be triggered by interruptions or suspensions to business. A common example of an event of default is where a borrower (or an obligor) 'ceases or threatens to cease to carry on all or a material part of its business'. Depending on the specific drafting, this may be triggered by the mandatory shutdowns in place (whether or not temporary). Be conscious that many loan facilities will also require borrowers to notify their financier of any potential event of default.

Evelyn Jones
Partner

D +64 9 905 1775
M +64 21 868 021
E evelyn.jones@laneneave.co.nz

Jacob Nutt
Associate

D +64 9 905 1763
M +64 21 0215 2262
E jacob.nutt@laneneave.co.nz

Stephanie Bode
Solicitor

D +64 9 905 1764
E stephanie.bode@laneneave.co.nz

- **Material adverse change**: Another common trigger for default is where a 'material adverse change' occurs in respect of a borrower (or an obligor). Generally, this includes the occurrence of an event that has a material adverse effect on the relevant person's business (financial or otherwise) or that person's ability to perform its obligations under the relevant loan and security documents. The subsistence of a 'MAC' may also operate as a drawstop under revolving facilities.
- **Reporting covenants**: Almost all loan facilities will contain reporting covenants, which require the borrower (or obligors) to regularly report to its financier(s) on certain matters. Most commonly, this will be financial statements and management accounts. Depending on the nature of the funding, borrowers may also be required to provide externally prepared information, such as property valuations prepared by a registered valuer. If borrowers foresee any issues meeting the reporting deadlines or obligations in their facilities (including due to internal or external resourcing issues or access to premises), they should contact their financiers.
- **Financial covenants**: Some loan facilities will contain specific financial covenants. These require borrowers (or obligors) to comply with certain financial measures to ensure that a borrower is able to comply with its obligations under the loan facilities. These measurements may be tied to a business' earnings or cashflow or the value of secured property. Some covenants may be tested 'at all times' whereas others may only be tested at scheduled intervals (for example, end of a financial quarter). If a borrower anticipates a breach, it should discuss with its financier(s), so that waivers or temporary suspension of testing can be agreed to avoid default.
- **Changes to pricing**: For some borrowers, facility agreement pricing will be tied to maintaining certain ratios, for example, in connection with their financial covenants, which may result in increased pricing.
- **Key contracts and counterparty default**: The continued availability of a facility may sometimes be tied to counterparty performance (e.g. contractors completing work in accordance with milestones under a construction contract, lessees not defaulting under lease agreements and so on). Any such provisions should be reviewed by borrowers, and any extensions or waivers required sought from the financier(s) as soon as possible.
- **Receivables financing**: Borrowers with receivables financing in place may need to monitor their receivables pools and ensure that receivables continue to meet any eligibility criteria and portfolio

parameters, in light of the potential for default by customers under those receivables. Likewise, any borrowers that rely heavily on receivables for cashflow will need to consider whether serviceability of a loan will be impacted by impaired recovery.

- **Shareholder funding**: Companies may be looking to their shareholders for additional funding. Loan facilities will most likely have restrictions on a borrower incurring debt (including a shareholder advance), without its financier's consent and subject to satisfactory priority and subordination arrangement required by its financier(s). If a borrower is looking to make any changes to its shareholder funding structure, it should contact its financier(s) to discuss.
- **Maintenance of secured property**: Borrowers will give financiers certain undertakings in relation to the property it grants security over. This will generally include an obligation to maintain its property in good repair and condition. Borrowers may need to consider the practical restrictions of gaining access to premises for this purpose during lockdowns. Again, if necessary, discuss any inability to meet these undertakings with your financier(s).

The key to addressing any issues that may arise will be to approach your financier(s) early, allowing all parties time to consider the best approach, and resolve any issues before they become insurmountable. Be aware that financiers may also be contacting businesses for more information than typically requested in order for them to assess the economic impacts of COVID-19 on your business(es).

For completeness, we note that the Farm Debt Mediation Act 2019 (FDMA) will come into force later this year, and provide for mandatory mediation before enforcement action can be taken in respect of 'farm debt' against those covered by the FDMA. For those in the farming sector, please see our earlier updates on the FDMA here to see if it will apply to your borrowing:

Farm Debt Mediation Bill Enacted (December 2019)
Farm Debt Mediation Bill (July 2019)

Our Banking and Finance team is here to help with all of your funding arrangements as New Zealand navigates COVID-19 – whether you are looking to borrow, restructure existing facilities, or would like assistance reviewing your existing loan facilities and obligations.