NON-BANK LENDER M&A

Guy Morgan and Stephanie Tsang of Fox Williams LLP discuss the key legal and commercial issues associated with the acquisition of non-bank lenders.

Non-bank lenders (NBLs) play a vital part in the global economy. These firms offer a variety of lending products, from business loans to small and medium sized enterprises (SMEs) to consumer loans for the retail market. It is estimated that approximately a third of money lent to SMEs in the UK comes from NBLs . This can, in part, be attributed to the fact that NBLs are, generally speaking, not subject to the same stringent prudential standards imposed by regulators on deposit-taking banks and can therefore make loans to high-risk customers.

The success of NBLs has made them appealing targets for acquisition, including by banks who are looking to scale or enter new markets, as well as other NBLs looking to consolidate their position int their chosen market. However, the acquisition of a non-bank lender presents a distinct set of legal challenges and regulatory considerations that differ significantly from the acquisition of a traditional trading business.

In this article, we examine the key elements of the process of acquiring or selling the entire issued share capital of a NBL (most of which apply also to making a significant (>25%) equity investment in a NBL).

Financing considerations

Many NBLs rely on wholesale funding arrangements such as securitisations, warehouse lending, or private credit facilities and/or may fund originations through forward flow arrangements. The terms of these financing arrangements must be reviewed as they are highly likely to contain change-of-control provisions that could be triggered by the acquisition, and so the implications of this must be worked through. Buyers must also assess the enforceability of the target's loan book, particularly if loan origination or servicing is outsourced.

If the NBL utilises special purpose vehicles (SPVs) or other group entities for funding purposes, the transaction structure will need to ensure that the funding arrangements (including any subordinated finance and any risk retention interests for securitisation regulatory purposes) remain intact post-acquisition as required. Where any debt facilities will not be replaced as part of the acquisition process, obtaining lender consents and ensuring continued access to funding lines will be critical for business continuity.

[1] https://www.ukfinance.org.uk/news-and-insight/blogs/crucial-role-non-bank-specialist-lender-sector-and-impact-covid-19

Examples of recent market activity

Date	Buyer	Target	Target's sector
2025	Spring Finance	Masthaven Finance	Bridging and development finance
2024	Allica Bank	Tuscan Capital	Bridge lending
2022	M&G	Finance Ireland	Residential mortgages, commercial property, car finance, leasing, SME financing and lending to the agricultural sector
2021	Starling Bank	Fleet Mortgages	Buy-to-let mortgage lender

https://iqeq.com/insights/rise-non-bank-lenders/

Management engagement terms and incentivisation

A strong management team is essential to the success of a NBL. A buyer will consider the suitability of the NBL's existing management team and whether the terms on which they are engaged sufficiently protect the business from the departure of a key individual.

This will involve a review of key employees' service agreements and any equity arrangements such as share option plans. The result of that review may be new service agreements with, for example, higher salaries, more restrictive non-compete provisions and/or longer notice periods, and/or the introduction of a new management equity incentive plan (which may or may not mirror the terms of any existing management incentive plan at NBL-level or making use of any existing scheme at buyer-level).

If a new management equity incentive plan is to be introduced, consideration will need to be given as to what form of scheme should be used in order to maximise any potential tax efficiencies while complying with the relevant legislation, such as growth share plans, company share option plans (CSOP) and joint share ownership plans (JSOP), bearing in mind that generally lending is an excluded activity for the purposes of the Enterprise Management Incentive (EMI) scheme.

Regulatory considerations

Unlike traditional banks, NBLs in the UK are not regulated by the Prudential Regulation Authority (PRA) for capital adequacy and liquidity purposes. However, they are frequently, but not always, authorised and regulated by the Financial Conduct Authority (FCA), particularly if they engage in consumer lending, mortgage lending, or credit broking. More often than not, NBLs will at least be registered with the FCA, for the purposes of anti-money laundering supervision.

Buyers must assess whether the target company holds the necessary authorisations to operate legally. Any gaps in authorisation could expose the acquirer to enforcement actions, fines, or operational restrictions. Furthermore, if the NBL has engaged in regulated activities without the appropriate authorisation, the enforceability of its loan agreements may be at risk.

If any applications have been made to the FCA or PRA for authorisation and have not been granted, buyers will generally include these applications and correspondence with the regulator within their due diligence in order to ascertain the reasons for authorisation being withheld / denied.

Additionally, a change of control of an FCA-regulated NBL (which, for the avoidance of doubt, does not include a NBL registered with the FCA for the sole purposes of supervising anti-money laundering) must be notified to the FCA before completion of the acquisition, and

Change of control

If applicable (see "Regulatory Considerations" heading), the regulatory change of control process generally comprises two stages:

1. **pre-notification** discussions with the FCA / PRA; and
2. the **notification** process. Once the notification has been submitted, the FCA / PRA has a statutory deadline of 60 working days beginning with the day on which the FCA / PRA acknowledges receipt of a complete notice.

In practice, the process can take longer than this because:

- The FCA / PRA can stop the clock at any point up to the 59th day to request further information and can extend the period by 20 or 30 business days (depending upon the status of the controller). As such, the FCA / PRA can have up to 90 working days (circa 4.5 months) in which to assess the change in control notification.
- It is not uncommon that the FCA / PRA do not acknowledge receipt and/or will deem applications incomplete (and so do not "start the clock" on the assessment period) for, at times, several weeks.

the buyer must obtain approval from the FCA if required. Failure to comply with these requirements could delay the transaction or lead to regulatory sanctions.

Business plan

In support of any regulatory change in control application, the buyer will generally need to prepare a business plan for the business.

Serious consideration will need to be given at an early stage to what the NBL's current regulatory business plan covers and whether this is compatible with the buyer's intentions for the business. Even if the buyer doesn't intend to amend the business model in any significant way, in all likelihood the current business plan will need to be updated simply because the existing business plan has become out of date over time. Any changes to the NBL's regulatory business plan will be considered carefully by the regulator.

Compliance with consumer protection laws

NBLs engaged in consumer and certain SME lending must comply with various regulatory obligations, including the Consumer Credit Act 1974 (as amended), the FCA's Handbook on both consumer credit (CONC) and mortgages (MCOB), and fair treatment of customers principles (in particular, Consumer Duty). Non-compliance can result in financial penalties, customer remediation obligations, and reputational damage. In the worst case scenario, the enforceability of the loans may also be at risk.

Buyers should review the target's lending agreements, policies, compliance and risk framework, and past regulatory audits to identify any potential legal exposure. Particular attention should be paid to high-cost short-term credit, affordability assessments, and adherence to the FCA's rules on forbearance and responsible lending. Vulnerable customers remain a hot topic for the FCA and buyers should satisfy themselves that appropriate processes have been in place to manage customers presenting with these characteristics.

Litigation and disputes

Given the regulatory scrutiny surrounding non-bank lending, buyers must conduct a thorough review of pending and historical litigation, including borrower complaints, mis-selling allegations, and regulatory enforcement actions.

Buyers should ensure that sufficient indemnities and warranties are included in the transaction documents to mitigate risks arising from pre-existing liabilities. In some cases, escrow arrangements or price adjustments may be necessary to account for contingent liabilities.

Warranties and disclosure

To provide assurance to the buyer of the value of the NBL, the transaction documentation will contain a list of warranties to be given by the sellers of the business.

All sellers will be expected to give 'fundamental' warranties relating to their title to the shares being sold and their capacity to enter into the transaction. In addition to that, some or all of the sellers will be asked to give business warranties.

Those business warranties will be tailored for the specific transaction but most likely will overlap with the areas of the buyer's diligence (including those items mentioned above) in order to confirm that the buyer's understanding of the business' operations is correct.

If there is a fact or matter that renders a warranty untrue, inaccurate or misleading, then those sellers who are providing business warranties would be expected to disclose this to the buyer (allowing the buyer to determine what impact, if any, such disclosure has on the transaction) or else risk suffering a breach of warranty claim.

Split exchange / completion

If the NBL is not regulated, the transaction can likely take place on a simultaneous exchange and Completion basis (i.e. closing happens as soon as definitive agreements are entered into) unless there is a specific reason requiring a split process.

If the NBL is regulated, given the length of time generally required for regulatory change in control approval (see table above), it is common for any relevant deals to be structured such that the transaction documentation is entered into upon agreement of key deal terms, the closing of which is dependent on receipt of the required regulatory approvals (aka a 'split exchange and completion').

Fox Williams financial services experience

Our multidisciplinary financial services sector group is recognised for providing effective advice to businesses in this competitive and highly regulated market.

We advise international and UK-headquartered banks (including challenger banks), non-bank lenders, insurers and investment firms, fintechs and payment platforms, as well as businesses seeking funding and those making investments in the sector.

Our expertise not only includes corporate transactions but also a wide range of specialist advice required by organisations and individuals working in financial services, including PRA and FCA regulation, business immigration, commercial disputes, employment law related issues, data protection and investigations.

Representative recent transactions our team have advised on include Allica Bank's 2024 acquisition of Tuscan Capital.

It is imperative that the deal documentation is clear as to how the parties will work together to obtain the change in control approval, how the parties will deal with any associated challenges (including conditions which may be specified by the regulator or the regulator simply refusing to provide the approval), and the circumstances in which a party can choose to terminate the transaction (for example if regulatory approval or deemed approval is not received by a certain date).

The parties will also need to consider to what extent they wish to agree to restrict the NBL's conduct between exchange and Completion (including any regulatory issues with the same) and/or deal with any change in the value of the NBL as between exchange and closing.

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