

# Financial litigation roundup

Winter 2016/2017

Welcome to the latest edition of our financial litigation roundup, which considers recent judgments, ongoing cases and legal developments from the banking and financial world in the UK and Asia. In this edition, we are also pleased to include a section covering developments in the offshore markets from our guest contributors, Appleby.

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### Law Reform Commission Sub-committee recommends third party funding for arbitration

The issue of third party funding for arbitration should be of particular interest to financial institutions, given the increase in the use of arbitration for disputes arising out of complex financial products such as derivative contracts, particularly in Asia. [more>](#)

### Tribunal orders sanctions for disclosure of false or misleading information

In November 2016, the Market Misconduct Tribunal formally handed down its orders in the "Citron Research" decision. [more>](#)

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Of the disputes involving investors and financial intermediaries that have gone to trial in Hong Kong since the global credit crisis in 2008, the banks have (for now) generally been able to rely on "boilerplate" type clauses to preclude an advisory duty arising, even if advice was given by a (for example) bank representative. [more>](#)

### Proposals to expand financial dispute resolution scheme

Hong Kong's Financial Dispute Resolution Centre (FDRC) opened in 2012. The FDRC operates a FDR Scheme, designed to give investors the option of a "one-stop" shop (and a "new deal") for the settlement of disputes between individual investors and financial institutions in Hong Kong. [more>](#)

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## Singapore case report

### *AAHG, LLC v Hong Hin Kay Albert*

In the context of dealings in equities, the Singapore High Court made significant observations relating to the law in Singapore on a claim for damage to reversionary interest as well as for restitutionary claims in unjust enrichment. [more>](#)

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## Active English cases of note for 2017

A heads up on significant banking and financial cases due before the English courts in the course of 2017. [more>](#)

## English judgments

### *BNY Mellon Corporate Trustee Services Ltd v LBG Capital No 1 Plc*

This appeal to the Supreme Court was brought by BNY Mellon in its capacity as the trustee under certain Enhanced Capital Notes (ECN) issued by Lloyds Banking Group (LBG). [more>](#)

### *Libyan Investment Authority v Goldman Sachs and ors*

The LIA is a sovereign wealth fund set up by the Gaddafi regime after the thaw in relations with Western powers and the lifting of sanctions on Libya in 2003/4. [more>](#)

### *O'Hare v Coutts & Co*

The claimants were a wealthy married couple, who had developed and sold a successful chemical engineering business. [more>](#)

### *Finch & Anor v Lloyds TSB Bank Plc & Ors*

This was a trial of two joined sets of claims. The dispute arose out of a loan agreement between Lloyds and a company called Bredbury Hall Limited (BHL) which had assigned its rights of action to the first claimant, Mr Finch. [more>](#)

### *Property Alliance Group Limited v Royal Bank of Scotland*

This case was long awaited in the London legal market. Two of the limbs of the case concerned aspects of banking conduct which have been subject to very public criticism and serious regulatory scrutiny. [more>](#)

### *Marme Inversiones 2007 S.L v Royal Bank of Scotland Plc & Ors*

This interlocutory judgment was given in relation to a jurisdictional challenge. [more>](#)

### *Exxonmobil Financial Services Limited v Lehman Brothers International (Europe) Limited*

EFMS had entered into tri-party repurchase (TPR) trades with LBIE, the main trading arm of Lehman in London, in the run up to the collapse of the Lehman group. [more>](#)

### *Flex-E-Vouchers Ltd v Royal Bank of Scotland (Mercantile Court)*

The defendant bank, The Royal Bank of Scotland Plc (RBS), brought an application against the claimant, Flex-E-Vouchers Limited. [more>](#)



## Offshore markets: Guest spot authored and contributed by Appleby

### ***UVW v XYZ (A Registered Agent) (BVI HC (COM))***

The Eastern Caribbean Supreme Court has broadened the scope of the jurisdiction to grant Norwich Pharmacal relief in the British Virgin Islands. [more>](#)

### ***Primeo Fund (in liquidation) v Herald Fund SPC (in liquidation)***

The status of redeeming hedge fund investors was addressed by the Cayman Islands Court of Appeal. [more>](#)

### ***Pearson v Primeo Fund***

In the same litigation as the case above, the Cayman Islands Grand Court has issued a further judgment on the power of a liquidator of a solvent Cayman Islands company. [more>](#)

### ***In the Matter of Up Energy Development Group Limited***

The Supreme Court of Bermuda has clarified the role of provisional liquidators in restructurings. [more>](#)

### ***Sonera Holding B.V. v Cukurova Holding A.S.***

The Eastern Caribbean Supreme Court has confirmed its jurisdiction to grant an injunction restraining a party from pursuing a foreign arbitration. [more>](#)

### ***Lime Petroleum Plc & Others***

The Isle of Man's High Court of Justice has concluded that the directors of a company can, at common law, without approval or support from the shareholders, pass a resolution for an insolvent company to be wound up and instruct advocates to file a winding up application on behalf of the company. [more>](#)

### ***Claims arising from the collapse of Providence and Lumiere***

The recent demise of Providence Global Ltd in Guernsey and the related independent financial adviser Lumiere Wealth Ltd in Jersey has generated much interest in the Channel Islands and elsewhere. [more>](#)

## Hong Kong legal developments

### Law Reform Commission Sub-committee recommends third party funding for arbitration

The issue of third party funding for arbitration should be of particular interest to financial institutions, given the increase in the use of arbitration for disputes arising out of complex financial products such as derivative contracts, particularly in Asia. Arbitration of such disputes is a viable alternative to litigation that should be explored; in particular, where the counterparty is in a jurisdiction in which enforcing a foreign Court judgment is challenging. While the banks tend to favour London or New York as the default option for disputes arising out of derivative contracts, for Asian counterparties Hong Kong and Singapore offer established disputes resolution hubs.

In October 2016 a Law Reform Commission Sub-committee published its much anticipated report on "Third Party Funding for Arbitration". As expected, the report came out strongly in favour of amending the Arbitration Ordinance (Cap. 609) to make it clear that third party funding of arbitration (and associated proceedings) under the Ordinance is permitted, subject to certain financial and certain safeguards. In particular, the report recommends that the Ordinance should be amended to make it clear that the crimes and torts of maintenance and champerty should no longer apply to arbitrations governed by the Ordinance.

Of particular note, the report recommends that:

- third party funding should not be provided by lawyers or those providing legal services
- in the interests of transparency, notice of third party funding should be given to each other party and the governing arbitration body
- for an initial period of 3 years, a "light touch" approach towards third party funding of arbitration in Hong Kong be adopted (as opposed to a statutory backed scheme); for example, pursuant to a Code of Practice dealing with ethical and financial standards that third party funders are expected to comply with.

Historically, the prospects of Law Reform Commission recommendations making their way onto the statute book in Hong Kong have not been good. However, the report's recommendations do generally have wide support in Hong Kong and "intel" suggests the government is supportive. It has not been lost on the government that Singapore (a competing disputes resolution centre) is moving ahead with its own proposals.

If the Law Reform Commission Sub-committee's proposals are to make their way onto the statute book then much will depend on the support of the local legal community; in particular, the relatively high concentration of lawyers in the legislative council (Legco) in order to attract cross-party support and to persuade certain "consumer" interests that third party funding for arbitration in Hong Kong is not a pretext to third party funding for litigation (ie, court disputes). Hong Kong already has statutory backed civil legal aid schemes protected by powerful lobby groups.

The Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Bill 2016 was introduced into the Legislative Council on 11 January 2017.

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### Tribunal orders sanctions for disclosure of false or misleading information

In November 2016, the Market Misconduct Tribunal formally handed down its orders in the “Citron Research” decision. The decision announced a couple of months earlier (in August) resulted in a finding that a “specified person” (a short seller) had made a financial gain on short selling stock in a Hong Kong listed company after having disclosed false or misleading information that induced transactions contrary to s. 277 of the Securities and Futures Ordinance (Cap. 571).

The sanctions ordered by the tribunal are civil sanctions (given that the proceedings are not criminal) but they are nevertheless tough. The tribunal ordered that the specified person (a resident of the US, not Hong Kong) be:

- banned from trading listed securities in Hong Kong for the maximum period of five years without prior permission of the court (a so-called “cold shoulder order”)
- subject to an order that he refrain from engaging in conduct so as to contravene section 277 of the Ordinance (a so-called “cease and desist order”)
- ordered to disgorge the profit said to have been made from short selling the shares of the listed company and repay the same to the government (together with interest for a specified period) and
- ordered to pay the government’s and the Securities and Futures Commission’s substantial legal costs (which far exceed the amount of the disgorged profit).

The tribunal’s decision to order the maximum period for a “cold shoulder order” says something about its opinion regarding the specified person’s degree of culpability. “Cease and desist orders” are not subject to a time limit.

The tribunal’s decision should also be seen in the wider context of regulators’ efforts to use a broad range of regulatory tools to challenge market participants who transgress in connection with the trading of shares listed in Hong Kong. The SFC itself has a number of ways it can combat different types of market misconduct, including – commencing civil proceedings in the High Court pursuant to section 213 of the Ordinance, initiating civil proceedings before the tribunal (as in this case) and assisting with investigations prior to criminal proceedings.

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### Amendments to SFC client agreement requirements in 2017

Going forward, the pretence whereby some banks and financial intermediaries make recommendations as to clients’ investments, but seek to rely on their acting on an execution only basis (in order to avoid liability) should become less prevalent in Hong Kong. The Securities and Futures Commission has mandated that by 9 June 2017 financial intermediaries governed by its Code of Conduct must include a new “suitability clause” in client agreements. The new clause includes a “non-derogation” provision. This will be complemented by a new provision in the Code of Conduct which will provide that a financial intermediary may not include in a client agreement any provision which is inconsistent with its obligations under the Code of Conduct or which misdescribes the actual services to be provided to a client.

As with previous occasions, the SFC has provided guidance on the client agreement regime by responses to FAQs; this time with respect to the application of the suitability clause. The SFC’s responses are understood to be further to queries raised by some financial institutions carrying

out (among other things) asset management activities and discretionary investment management services. The responses seek to clarify the limited circumstances in which a financial intermediary can waive the need to enter into a client agreement or is entitled to rely on exemptions.

As for the practical issue of how best to update existing client agreements (for example, by way of amendment or replacement) in order to make them compliant with the new provisions, the SFC's response suggests that intermediaries "seek legal advice on this if in doubt". Options include a negative consent approach or re-execution of client agreements.

Besides the new suitability clause (for client agreements), suitability obligations are already the cornerstone of regulatory protection for investors in Hong Kong, pursuant to paragraph 5.2 ("Know your client: reasonable advice") of the SFC's Code of Conduct. In this regard, the SFC has recently issued further guidance by way of responses to FAQs. The responses seek to give guidance to licensed or registered persons concerning the discharge of their obligations under paragraph 5.2 of the Code of Conduct; including, in particular, guidance on the circumstances in which these obligations may be triggered.

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### ***Chang Pui Yin & Ors v Bank of Singapore Ltd: Investor succeeds with claim against bank***

Of the disputes involving investors and financial intermediaries that have gone to trial in Hong Kong since the global credit crisis in 2008, the banks have (for now) generally been able to rely on "boilerplate" type clauses to preclude an advisory duty arising, even if advice was given by a (for example) bank representative. The banks have (in the main) been successful in arguing that they act on an execution-only basis. It is against this background that the Securities and Futures Commission had mandated the amendments to the client agreement regime for financial intermediaries governed by its Code of Conduct (see above).

*Chang Pui Yin & Ors v Bank of Singapore Ltd* [2016] HKEC 1721, HCCL 12/2013 is the latest "investor" claim against a bank to go to trial in Hong Kong. It is a rare case of investors succeeding in establishing that (as a matter of contractual interpretation) the bank owed them an advisory duty; in particular, a duty to act with reasonable care and skill in recommending investment products for their investment portfolio held with the bank. Based on the evidence at trial (on the issue of liability, with quantum to be assessed) the investors also succeeded in establishing the bank breached that duty by over exposing them to high risk investments.

It should be stressed that the investors were an old couple and unsophisticated in matters of financial investment. Crucially, they were able to demonstrate that they had placed trust in and reliance on the bank representative's advice and that, on the facts, the bank's general disclaimer did not apply.

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### **Proposals to expand financial dispute resolution scheme**

Hong Kong's Financial Dispute Resolution Centre (FDRC) opened in 2012. The FDRC operates a FDR Scheme, designed to give investors the option of a "one-stop" shop (and a "new deal") for the settlement of disputes between individual investors and financial institutions in Hong Kong. The scheme has its origins in the government's wish to be seen to be assisting retail investors in connection with the sorts of misselling practices that gave rise to the so-called "Mini-Bonds" saga in Hong Kong, just after the credit crisis in 2008.



All financial institutions regulated by the SFC (but excluding credit rating agencies) or authorised by the Hong Kong Monetary Authority are required to participate in the scheme. Currently, the amount of a financial claim that comes within the scheme is HK\$500,000 (or the foreign currency equivalent). The claim must also be made within 12 months from the date of the purchase of the financial service (or product) or the date on which the claimant first had knowledge of their monetary loss arising out of the financial service (or product).

The FDRC is undertaking a public consultation to enhance the scheme. Two of the key proposals include increasing the monetary jurisdiction of the scheme to HK\$3m and extending the limitation period in which to commence a claim to three years. These are significant proposals.

It will be interesting to see how the proposals progress. While the scheme has largely been a success, from the view point of consumers, there have been concerns that some claims are “over-mediated” and that some financial institutions pay lip-service to the scheme.

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## Hong Kong law Anti-Money Laundering “stocktake” 2016

Developments in 2016 included:

- well before the year end, Hong Kong broke its “personal best” for the number of suspicious transaction reports (STRs) made in one year. In 2015, the figure was 42,555 STRs. For 2016 the Joint Financial Intelligence Unit website showed that 76,590 STRs had been made. The vast majority of STRs are (of course) made by the banks
- while the number of convictions for money laundering activities (and the amount of assets restrained and recovered by the relevant authorities) is likely to be lower in Hong Kong for 2016, compared with the previous few years, this can be explained. For example:
  - first, some prosecutions may have been delayed pending important clarification by the Court of Final Appeal concerning the law relating to the offence of dealing with property knowing or having reasonable grounds to believe that it represents the proceeds of a serious crime; in particular – (i) the meaning of “reasonable grounds” as an alternative to knowledge ; and (ii) confirmation that conduct committed overseas is caught by the “dealing” offence, if such conduct constitutes a serious offence in Hong Kong (regardless of the legal position in the jurisdiction where the conduct took place)
  - second, a greater level of reporting suggests a better awareness of money laundering risks. Indeed, there have been complaints within the business community in Hong Kong that some international banks have overdone their customer due diligence requirements, such that opening bank accounts for SMEs in Hong Kong has become too difficult
- in the run-up to the Financial Action Task Force’s next mutual evaluation of Hong Kong (in 2018-19) investigative agencies and regulators are expected to turn their attention to certain non-financial institutions, such as (for example) company service providers and auction houses, and to the so-called “shadow banking” industry.

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## Singapore case report

### **AAHG, LLC v Hong Hin Kay Albert [2016] SGHC 274**

#### **Case summary**

In the context of dealings in equities, the Singapore High Court made significant observations relating to the law in Singapore on a claim for damage to reversionary interest as well as for restitutionary claims in unjust enrichment.

#### **Brief facts**

The Defendant Albert Hong (Hong) and an American company DVI, Inc. (DVI) held shares in a Singapore-incorporated company Universal Medicare Pte Ltd (Universal). The central allegation made against Hong was that he had converted the 10,000 shares registered in DVI's name (the Shares) to his own use sometime in December 2007 and had thereafter sold these shares and pocketed the proceeds in January 2008.

DVI, acting through its trustee in liquidation, had commenced proceedings against Hong asserting a claim for damages for conversion or, alternatively, a restitutionary claim in unjust enrichment. The Plaintiff, AAHG, LLC (AAHG) subsequently acquired all of DVI's rights in relation to the Shares, including the rights in relation to the claim against Hong.

Hong denied the allegation of conversion, claiming he obtained the Shares pursuant to an exercise of pre-emption rights afforded him under Universal's Articles of Association. Alternatively, he claimed that DVI had pledged the shares to a third party at an earlier date and therefore that he did not have the requisite possession or right to immediate possession of the Shares at the time of the alleged conversion. He also claimed that the restitutionary claim was unsustainable as AAHG had not identified what it claimed was the unjust factor.

AAHG denied that the Shares had been pledged at any time, and asserted that DVI therefore had the requisite right to immediate possession of the Shares at the time of conversion. Alternatively, it asserted that even if the Shares had been pledged, DVI retained a reversionary interest in the Shares and Hong's conduct had caused it to suffer damage to that reversionary interest for which it was entitled to recover damages.

On the restitutionary claim, AAHG asserted that DVI's lack of consent to the transfer of its shares to Hong was a sufficient unjust factor for the purposes of establishing its claim in unjust enrichment.

#### **The Court's decision**

##### *Reversionary interest claim*

The Court found that the Shares had not been pledged to a third party and that DVI therefore had the requisite right to immediate possession necessary to found a claim for conversion.

The Court found that Hong was not entitled to the Shares, whether pursuant to an exercise of pre-emption rights or otherwise, and therefore allowed the claim for conversion and awarded a sum of just under S\$2.5m in damages.

The Court also found that even if the Shares had been pledged, DVI would have been entitled to bring a claim for damage to its reversionary interest in the Shares. In doing so, the Court recognised such a claim as a separate and distinct cause of action available to DVI. This essentially follows the position adopted in the England, where the Courts have described such

claims for damage to reversionary interests as being essentially “ancillary or parasitical to the principal tort to which it relates”. In this case, the Court held that such a claim was ancillary to the principal claim in the tort of conversion.

*Unjust enrichment claim*

The Court also found that the unjust enrichment claim had been made out. The Court accepted Hong’s argument that AAHG was required to specifically identify the “unjust” factor it was relying on and that such an “unjust” factor had to fall within the list of recognised unjust factors or events in order to give rise to a claim for unjust enrichment. However, the Court also accepted AAHG’s argument that DVI’s lack of consent in respect of the transfer of its shares to Hong was sufficient to satisfy the requirement for an “unjust factor”.

In doing so, the Court for the first time expressly recognised that such lack of consent as an “unjust” factor for the purposes of a claim for unjust enrichment.

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## Active English cases of note for 2017

### **The Libya Investment Authority's claim against Societe Generale**

The Libyan Investment Authority is bringing a claim against Societe Generale for \$2.1bn in relation to derivative trades it advised the sovereign wealth fund to enter into. The case is due to be heard in Spring 2017, and involves serious allegations of bribery. (The judgment in the unsuccessful parallel claim brought by the LIA against Goldman Sachs is reported on below)

### **UBS AG v Kommunale Wasserwerke Leipzig Gmbh**

One of the most significant cases of 2014 heads for the Court of Appeal in mid-2017, with permission to appeal having been granted on the widest basis it is set down for a two week hearing.

### **LBIE waterfall cases**

As the administration of the London arm of Lehman Brothers group draws to a conclusion, a set of three cases are due to be heard in the course of this year to determine the order in which surpluses are to be allocated from LBIE (the former principal trading arm) to other entities in the Lehman Group.

### **RBOS Shareholders Action Group v RBS & ors**

The prospectus claims against RBS and its former directors are due to reach trial of liability issues in March. Following the initial failure of a two day mediation which was widely leaked to the press in July 2016, four of the original five claimant groups had reached a settlement with RBS by early January. The RBS Shareholders Action Group, representing 27,000 claimants including many individuals as well as institutional clients, has yet to do so.

### **National Bank Trust v Ilya Yurov & Others**

National Bank Trust is seeking damages of around \$850m from its former shareholders in a dispute sparked by the Russian bank's collapse in 2014. The new owners of the bank allege that the former shareholders diverted over \$1bn of the bank's funds through loans to their own personal companies. An \$800m freezing order has already been issued, with the judge branding what the defendants had described as "balance sheet management" as instead being a "Ponzi scheme with a fancy name".

### **Fortress & Others v BNP Paribas & Others**

This case is listed for trial in the Commercial Court in October. It stems from the collapse of the Saad group in 2008. This litigation concerns a \$650m Sukuk transaction entered into with Maan al-Sanea, the chairman and principal of the Saad Group. The Trustee (Golden Belt 1 Sukuk Company) and various hedge fund investors are suing BNP Paribas (as arranger, manager and bookrunner) for damages arising from its alleged failure to obtain a signature on the deal documentation from Maan al-Sanea in the "wet ink" form necessary to make it binding in Saudi law (with the result that Saudi proceedings against Maan al-Sanea are unlikely to give any recovery).

### **Bank Mellat v HM Treasury**

The Iranian Bank Mellat's claim against the UK government stemming from imposition of sanctions is set to reach trial in November of this year. The long running dispute saw Bank Mellat lose a succession of hearings before the UK courts before enjoying a reversal of fortunes in the ECJ, which ruled that it was not a state-owned institution. The case has now been remitted to the High Court for an assessment of damages.

## English judgments

### ***BNY Mellon Corporate Trustee Services Ltd v LBG Capital No 1 Plc and another [2016] UKSC 29***

#### **Case summary**

This appeal to the Supreme Court was brought by BNY Mellon in its capacity as the trustee under certain Enhanced Capital Notes (ECN) issued by Lloyds Banking Group (LBG). The ECN had been issued by LBG in the wake of FCA stress tests conducted in 2009, following which LBG was ordered to raise an additional £21m of Core Tier 1 capital. LBG did so through issuing £8.5bn of ECNs in an exchange programme for existing securities, and through a £13.5bn equity rights issue. Although the ECN were not themselves Core Tier 1 capital, as contingent convertibles (Cocos) their terms provided that if LBG's Core Tier 1 capital ratio fell below 5% (of risk weighted assets) then they would convert into equity (creating additional further Core Tier 1 assets). At the time, the FSA (following the then current Basel II and EU regulatory standards) took account of Cocos in assessing the key "Consolidated" Core Tier 1 ratio.

There were various series of notes in the ECN programme with terms lasting to between 2019 and 2032, carrying varying rates of interest which averaged at an expensive 10.33% pa. The trust deed also provided that LBG could redeem the ECNs early if a "Capital Disqualification Event" occurred. The terms provided that such an event would arise if "the ECNs shall cease to be taken into account in whole or in part ... for the purposes of any "stress test" applied by the FSA in respect of the Consolidated Core Tier 1 Ratio".

In 2013, the FSA was abolished and the relevant parts of its powers was passed to the then new Prudential Regulation Authority (PRA) under the control of the Bank of England. Meanwhile, Basel III, and the resulting revised EU Capital Requirements Directive, changed the basis for assessing banking capital adequacy. The concept of "Core Tier 1" capital was replaced by the more restrictive concept of "Common Equity Tier 1" capital (CET1 Capital), and the introduction of a new category of Additional Tier 1 capital (AT1 Capital) which included Cocos which met qualifying conditions as to the capital adequacy ratio at which they would convert into equity.

Following these regulatory developments, LBG sought to adjust its capital structure. As part of that LBG made an offer to exchange the ECNs for new Cocos which would meet AT1 Capital requirements and so be taken into consideration in future CET1 Capital stress testing. £5bn of the £8.5bn of ECN were exchanged, but this left a substantial rump of hold-outs.

In April 2014, the Bank of England issued guidance to the PRA which increased required CET1 Capital ratios to 7% of risk weighted assets. The PRA subsequently determined that Cocos would only be considered as AT1 Capital if they were convertible into equity upon the CET1 Capital ratio falling below a level of 5.125%.

In December 2014 the PRA reported that LBG's actual CET1 Capital ratio at the end of 2013 had been 10.1% and that under stress tests this was projected as falling to 5%. The ECNs had not been taken into any consideration by the PRA in these calculations, because they would only be convertible into equity if the CET1 Capital ratio fell to 1% and so were irrelevant to whether the CET1 Capital ratio would fall below the required levels.

Shortly afterwards, LBG announced that the PRA had not taken account of the ECNs in the December 2014 stress testing and that this comprised a Capital Disqualification Event as a result of which LBG was redeeming the ECNs.

On behalf of the Noteholders, the Trustee sought to challenge the Issuer's attempt to redeem the ECNs on this basis. The Trustee succeeded at first instance, but that decision was overturned by the Court of Appeal. The Trustee then appealed to the Supreme Court, and lost by a majority decision with two dissenting judgments.

The Trustee ran two lines of argument. The first was that a Capital Disqualification Event had not occurred because such an event related to a consolidated Core Tier 1 ratio, which was a defunct concept which had been replaced by the CET1 Ratio. This argument was dismissed unanimously. The majority held that the investors in the ECN could be assumed to have been aware of the regulatory concepts which drove the convertibility and redemption provisions in the ECNs, and would have been cognisant of the potential that those would develop over time. The change from Core Tier 1 Capital to CET1 Capital was merely nomenclature.

The second argument run by the Trustee was the one which had found favour at first instance and with which the dissenters in the Supreme Court agreed. The majority judgment acknowledged it was a difficult question to resolve. This was, in essence whether it was correct to say that the PRA (as successors to the FSA) had in fact "not taken into account" the ECNs in the stress test calculations, or, rather, as the Trustee argued, whether the PRA had taken them into account by considering whether they contributed to the passing or failing of the stress test, but concluding that they did not. As Lord Sumption in dissent put it, the question was whether in order to be taken into account, the stress testing had to include an assumption that the ECNs "would convert and play a part in enabling the Bank to pass the stress test". The majority found that the regulatory changes had meant that the ECNs could not be and were not taken into account by the PRA in assessing whether the stress test was passed.

The findings are quite particular to the terms of these particular notes. Although not forging new law, two points of more general application were made:

- within the context of sophisticated financial instruments such as the ECNs, it was appropriate to assume that the parties understood the basic regulatory framework and the commercial purpose of the ECNs within that context. Subject to that, the Trust Deed was to be interpreted from its wording, and in particular it was not found to be helpful or appropriate to refer to the Offering Memorandum as a guide to contractual interpretation
- in response to submissions that the Trust Deed had been drafted by the Issuer and should be read against LBG where there was a lack of clarity, it was held that "the contra proferentum rule is very much a last refuge, almost an admission of defeat, when it comes to construing a document" and that it would be unnecessary and inappropriate to resort to it.

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### ***Libyan Investment Authority v Goldman Sachs and ors [2016] EWHC 2530***

#### **Case summary**

The LIA is a sovereign wealth fund set up by the Gaddafi regime after the thaw in relations with Western powers and the lifting of sanctions on Libya in 2003/4. By early 2008 the LIA had at least \$30bn of assets to manage, and an expectation that substantial sums would continue to be paid in annually. As such, the LIA was a valuable potential client, whose business was hotly pursued. Among its suitors was Goldman Sachs, the defendant to the LIA's claims.

In early 2008 the LIA entered into nine leveraged derivative transactions with Goldman Sachs (the Disputed Trades). The Disputed Trades comprised a put option combined with a forward

purchase each with around a three year term, giving the LIA a leveraged exposure to the price action of the reference shares over that period. Each transaction related to the shares in a single company, across a range of blue chip stocks in the banking and financial, and energy sectors. The trades were entered into at a time when share prices had fallen sharply off their pre-crisis peaks, but before the 2008 financial crisis had gathered its full momentum. By each trade, the LIA paid a lump sum premium in advance to Goldman Sachs. If the share price increased over the three year term, Goldman Sachs would pay to the LIA the leveraged uplift in the value of the reference holding. If the share price did not increase, Goldman Sachs would retain the premium and the LIA would receive nothing. The total value of the premiums paid to Goldman Sachs amounted to around \$1.2bn.

In the proceedings, the LIA sought to rescind the Disputed Trades and to obtain repayment of the premiums from Goldman Sachs. The LIA's claim was based on two causes of action. The primary claim was that Goldman Sachs had procured the LIA to enter into the Disputed Trades by the exercise of undue influence over the LIA. The second claim was that the Disputed Trades were unconscionable bargains (i.e. transactions in which a party had exploited the weakness of another party in a morally culpable manner with overreaching and oppressive results).

In relation to certain transactions in April 2008, the LIA asserted that Goldman Sachs had exerted undue influence over it by means of offering and providing an internship to the brother of one of the key LIA decision makers. The LIA's position was that this key decision maker was induced into signing off on those transactions by this offer of familial advancement, after signs that LIA and the decision maker had been cooling on the idea of entering into them, as very shortly after the internship arrangements were made the trades in question were agreed. The LIA argued that this inducement was sufficient to raise a presumption of undue influence.

In wider terms, the LIA alleged that a relationship of trust and confidence had been built between the LIA and Goldman Sachs, which had gone beyond the usual commercial relationship between a bank and its client. The claims rested on LIA's assertion that it and its staff were naïve and unsophisticated in financial terms, did not understand the trades they were entering into, and that it had entrusted its affairs to Goldman Sachs which had then unfairly taken advantage of the trust that LIA had reposed in it. The LIA claimed that it had (mistakenly) trusted Goldman Sachs to act in the LIA's best interests when advising it, even where that conflicted with Goldman Sachs' own commercial best interests. This, the LIA argued, meant that a "protected relationship" had been created between LIA and Goldman Sachs, such a protected relationship being a necessary precursor to establishing any claim to set aside transactions for undue influence (which cannot be invoked for ordinary arms-length commercial relationships). In large part, this protected relationship of trust and confidence was said to have arisen because Goldman Sachs had more or less embedded a salesman at LIA's office in Tripoli, although the LIA relied on a range of other factors as well. The LIA also then argued that Goldman Sach's profits were so excessively large that they should be presumed to have been obtained by undue influence.

Mrs Justice Rose rejected all of LIA's claims. She found the internship provided by Goldman Sachs had been a marketing tool, but held that it had not materially influenced the LIA's decisions to enter into the April 2008 trades. More widely, she did not accept that the LIA was as unsophisticated and unaware of the nature of the transactions it had entered into as it claimed to be, and found that there was no "protected relationship" between the LIA and Goldman Sachs. She held that the "relationship did not go beyond the normal cordial and mutually beneficial relationship between a bank and a client. Goldman Sachs did not become a trusted

adviser or a "man of affairs" for the LIA". Nor did she accept that Goldman Sachs had deliberately manipulated or withheld information from the LIA, or that it had made excess profits on the deals.

We understand that LIA is seeking leave to appeal.

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### O'Hare v Coutts & Co [2016] EWHC 2224 (QB)

#### Case summary

The claimants were a wealthy married couple, who had developed and sold a successful chemical engineering business. Following the sale, the claimants entered into five investments in hedge funds in 2007, 2008 and 2010 on the advice of the defendant, Coutts.

The claimants issued proceedings alleging that the investments were unsuitable for their risk profile and that Coutts had breached a duty of care owed to them. They pleaded causes of action based on breach of contract (based on breach of an implied duty to advise with reasonable skill and care), negligence, breach of statutory (regulatory - conduct of business) duty and negligent misrepresentation. The quantum of their claims was put at around £3.3m, plus interest.

Coutts defended the claim stating that the investment advice was sound and the investments suitable for the couple. It submitted that the complaints of poor performance were informed by hindsight, and that the couple's risk appetite had in fact been higher than was now being claimed. In addition, the bank argued that Mr O'Hare was an "experienced investor" and was capable of reaching his own decisions without reliance on Coutts' relationship manager and sales personnel.

The court held that there was no breach of duty in contract or tort and dismissed the claim in its entirety.

In doing so, Kerr J held that the Bolam test which is ordinarily the required standard of care (acting "in accordance with a practice accepted as proper by a responsible body of...men skilled in that particular art") was not the appropriate test to apply in the context of a private banker/client relationship. This, Kerr J held, was because there is little consensus in the financial industry as to "how treatment of risk appetite should be managed by an adviser", and so the question should not be framed in terms of whether a reasonable adviser would have recommended the particular investment in question. Instead, the judge held it was more appropriate to apply the test of negligence developed to assess whether the risks benefit analysis of a proposed medical procedure had been competently given to a prospective patient (the "Montgomery" approach), which focuses on whether "reasonable care has been taken to ensure that a reasonable person is aware of any material risks ... and of any reasonable alternative or variant treatments".

On this basis, the judge found no substantive difference in the duty of care owed by Coutts under the relevant causes of action. He then held that "there is nothing intrinsically wrong with a private banker using persuasive techniques to induce a client to take risks the client would not take but for the banker's powers of persuasion, provided the client can afford to take the risks and shows himself willing to take them, and provided the risks are not – avoiding the temptation to use hindsight – so high as to be foolhardy. The authorities include mention

of the adviser sometimes having to save the client from himself, but also of the principle that investors take responsibility for their investment decisions including mistaken ones. The duty of care must reflect a balance between those two propositions, which pull in opposite directions." On that basis, the judge held that competent practitioners would not have regarded the investments in dispute as foolhardy for the O'Hares, and found that the risks and upside had been competently and sufficiently explained so as to make it fair to attribute responsibility for the entry into the transactions to the O'Hares, notwithstanding the persuasive influence of the Coutts' salesman.

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### ***Finch & Anor v Lloyds TSB Bank Plc & Ors [2016] EWHC 1236***

#### **Case summary**

##### **Facts**

This was a trial of two joined sets of claims. The dispute arose out of a loan agreement between Lloyds and a company called Bredbury Hall Limited (BHL) which had assigned its rights of action to the first claimant, Mr Finch. Lloyds had made a fixed interest rate loan facility available to BHL for up to £11.6m for a term of 10 years. Under the agreement, BHL was obliged to make good any break costs incurred by Lloyds as a result of an early repayment. On the claimants' version of events, after the agreement was entered into, Lloyds told BHL's directors that these break costs would include the costs of unwinding an interest rate swap agreement the bank had entered into in order to hedge its interest rate risk and were said to be likely to exceed £1.5m.

The claimants alleged that Lloyds had breached its duty in both contract and in tort to advise it as to the existence of any onerous terms in the Loan Agreement, and that Lloyds had negligently misrepresented that the Loan Agreement had been tailored to BHL's needs. The claimants alleged that Mr Finch had informed the Lloyds relationship manager that BHL would wish to repay the loan early due to ages of its investor principals, and that the break costs were prohibitive to this.

The court found that the Bank had no contractual or tortious duty to advise the Claimants about the terms of the Loan Agreement. HHJ Pelling stated that the claim had not been advanced on the basis that advice had been sought and was negligently wrong, but rather on the basis that advice had not been volunteered by the bank (advice which might have been contrary to the bank's own commercial best interest). The judge found that this alleged duty to volunteer suitability advice went further than any previous authority, and was contrary to the general principle that a bank is under no legal obligation to provide advice but if it does it must do so with reasonable care and skill. If such a duty was to arise, the circumstances would have to be "exceptional and markedly different from the conventional relations of banker and customer". That was not found to be the case.

In relation to the misrepresentation claim, the judge accepted that the Bank had been told at the outset of the relationship that early repayment would be likely to be made due to the age of the principals, but held that at that stage that was only expression of intention rather than one of fact. Furthermore, he found that the statement that Lloyds had "tailored" the loan terms to BHL's requirements did not mean they were an exact match, but that the loan terms offered were what the Bank was prepared to offer when considering the requirements that had been given to it.

In the second claim (the Guarantee Claim) the claimant, Promontoria Holding BV (PHBV) pursued a claim for monies due under guarantees given to Lloyds by the investors in BHL over performance of part of the loan facility. The defence to this rested on the same grounds as the first claim and failed in the same manner. In addition, the defendants alleged that Lloyds had agreed that the guarantees would be discharged or not enforced if the LTV under the loan agreement fell below 70%. The court dismissed this estoppel argument on the basis that although Lloyds had made the promise, the loan agreement which had subsequently been signed included a non-reliance clause which provided that the parties had not relied on any representations or statements made outside the walls of the loan agreement, and that the defendants could not therefore establish any reliance on the pre-contractual statement from Lloyds.

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## ***Property Alliance Group Limited v Royal Bank of Scotland 2016 EWHC 3342 (Ch)***

### **Case summary**

This case was long awaited in the London legal market. Two of the limbs of the case concerned aspects of banking conduct which have been subject to very public criticism and serious regulatory scrutiny: LIBOR manipulation, and the actions of RBS's Global Restructuring Group in dealing with distressed business customers in the wake of the 2008 crisis. This case was the first time a civil court has been asked to reach a judgment at trial on matters within these very well publicised issues of concern.

Property Alliance Group Limited (PAG) is a property investment company. Its primary banking relationship was with RBS until PAG severed relations in 2015. The litigation concerned four interest rate swaps (the Swaps) which PAG entered into with RBS in the period between 2004 and 2008, in connection with floating rate lending also provided by RBS. There were three core limbs to the case, as set out below.

### **The LIBOR issues**

The Swaps were all referenced to 3 month GBP LIBOR. PAG sought to argue that RBS in offering to enter into such transactions had made implied representations about the setting of LIBOR, which it claimed were in fact false misrepresentations because (it claimed) RBS had engaged in manipulating the LIBOR rate by making false submissions to the BBA.

In summary, PAG submitted that RBS had impliedly represented (a) that LIBOR rates (generally) would be determined as envisaged by the BBA methodology and accordingly would be an accurate reflection of the average borrowing rate faced by the panel banks (b) that RBS had no reason to believe that LIBOR rates (generally) were not an accurate reflection of the LIBOR panel bank funding costs in those currencies and tenors (c) that RBS had not and would not in the future make false or misleading LIBOR submissions or attempt to manipulate LIBOR rates (in any tenor or currency).

In the alternative, PAG argued that equivalent terms should be implied into the contracts, but narrowed to relate to the contractual 3 month LIBOR rate. This was in order to try to establish a back-stop entitlement to a lesser damages remedy, if the misrepresentation claims (with the more valuable remedy of rescission of the contract) failed.

Both these claims failed on all bases. First, the judge found that RBS offering to enter into LIBOR swaps was not sufficient conduct from which PAG could have inferred any implied representations. Secondly, she found that the pleaded alleged implied representations

were too technical to have been inferred, even if there had been any conduct giving rise to implied representations. At the highest, the judge considered that a much narrower implied representation might have been inferred if there had been sufficient conduct to warrant it: this would have been limited to a representation that 3 month GBP LIBOR rate would be set in accordance with the BBA definition. Thirdly, she found that PAG had not relied on the alleged misrepresentations, as the relevant PAG decision makers had not considered the LIBOR reference rates at the level of detail they would have needed to in order to rely on the technical alleged implied terms.

The court proceeded to find that PAG had not established on the balance of probabilities that RBS had in fact manipulated or made false submissions in respect of GBP LIBOR. The judge refused to draw any inferences from the fact that RBS had admitted to making false CHF LIBOR and JPY LIBOR submissions (admissions made originally in US Department of Justice proceedings). As no such conduct had been established in relation to GBP 3 month LIBOR, there was no breach of the implied term and nor on that basis was any narrowed implied representation which might have arisen a false representation.

#### **The other misselling claims**

PAG also sought to rescind the Swaps on the basis that they were missold for other reasons. In summary, PAG complained that it had been provided with incomplete and misleading information on matters such as break costs, and that the Swaps had been sold to it as suitable hedges against the interest rate risks on its floating rate loans but were unsuited for that due to factors such as maturity mismatch and built-in one-way cancellation rights in favour of RBS.

It was common ground that RBS did not owe a general duty to advise PAG in relation to the Swaps, and that the relevant contracts prevented PAG from arguing to contrary by setting up contractual estoppels.

Based on the chain of authority which can be traced through Bankers Trust and into the 2015 case of Crestsign NatWest, PAG pleaded that it was owed a “mezzanine” duty of care by which, through volunteering some information on the proposed Swaps, RBS had assumed a duty to explain the nature of those transactions fully and accurately, correcting any obvious misunderstandings on PAG’s part and answering any reasonable questions. The judge rejected any contention that the offering of some information by a bank would place a bank salesman under a duty fully to explain the transaction irrespective of whether there was a general duty to advise. The inquiry was much more fact sensitive, and in this case, the judge found that no such duty arose for a variety of reasons including PAG’s relative sophistication, its utilisation of financial advisors, and the fact that standard market practice was not to disclose detailed information about break costs. Moreover, even if there had *prima facie* been such a duty, it would have been set aside by the non-reliance clauses in the subsequent transaction documents.

In relation to the more specific allegations of misrepresentations, there were also found to be barred by the non-reliance clauses. The use of the term “hedge” was held to be a generic term, which did not carry with it a specific representation that the product would be a suitable means of laying off all of the particular floating rate interest rate risks which PAG faced. Nor, the judge held, did PAG in fact consider that the Swaps achieved this end of a true perfect hedge; and as its key decision makers did not believe they were such a thing, it followed that PAG could not have acted in reliance on any representation that they were.

### The GRG claims

The GRG claims concerned the actions which RBS took in transferring it to its GRG distressed lending unit and thereafter in managing the relationship with PAG. The claims rested on the contentions that RBS was under an implied duty to (i) act in good faith and in a commercially acceptable manner towards PAG or (ii) to exercise any discretion rationally and in good faith.

The court declined to imply a term into the contract obliging RBS to act in good faith. No such duty of course exists in English law by default, and it is necessary to establish that such a term should be implied into a contract on the usual principles. In this case, the court held that it was unnecessary to do so to reflect the intentions of the parties or to ensure business efficacy, and that such a term should not be implied into standard banking documentation. In relation to the exercise of discretion, the court found that the relevant powers that RBS had been exercising were unilateral entitlements under the contracts, and thus that there was no necessary purpose in implying a term which controlled the manner of exercise of a discretion conferred on RBS. Moreover, the court found that even if these terms had been implied, none of the actions of which PAG complained constituted bad faith or irrationality.

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### *Marme Inversiones 2007 S.L v Royal Bank of Scotland Plc & Ors [2016] EWHC 1570*

#### Case summary

This interlocutory judgment was given in relation to a jurisdictional challenge. The proceedings are part of a wider dispute relating to a finance package entered into as part of a £2bn sale and leaseback of Santander's global headquarters in 2007. Marme Inversiones (Marme) was an SPV incorporated in Spain as the acquisition vehicle. The purchase was financed by a £1.6bn floating rate syndicated senior loan facility with a 5 year term, with RBS being the lead arranger. Five of the syndicate banks also entered into interest rate swap agreements with Marme, under which Marme was to be a fixed rate payer for a term of around 15 years.

The 5 year term of the senior loan facility expired in 2013. Marme was unable to find replacement finance, and defaulted on its repayment obligations. Marme was placed in a Spanish voluntary insolvency procedure and subsequently went into liquidation. The following claims were issued:

- in June 2014, the lending syndicate issued a claim in the Spanish insolvency proceedings, objecting to the administrator's proposed way of dealing with payments due from Marme under the swaps. Marme counterclaimed in these proceedings for a termination of the swaps
- in September 2014, Marme filed a claim in the English courts for rescission for the swaps on the basis of alleged implied misrepresentation by RBS, based in the European Competition Commission's finding that RBS had participated in a cartel which had manipulated the EURIBOR rate (against which the swaps and senior loan facility were referenced). The banks issued counterclaims in this action
- in December 2014, RBS issued a claim in the English court for declarations that it had lawfully terminated its swap by notice served in November 2014 and that the close out amount specified by RBS was due.

Marme sought to stay both RBS's declaratory proceedings and the bank's counterclaims in its own English law rescission action (but not its rescission claim, which it sought to continue to pursue), pending the determination of the Spanish claim and counterclaim. Its position was that all three of the above proceedings were related actions under Article 28 of the Brussels Regulation, and that the Spanish court was first seised.

The English court declined to stay the English actions on the basis that the actions were not sufficiently related for the purposes of Article 28. It found that these actions concerned the validity, meaning and operation of the English law contracts. The Spanish proceedings concerned the application of provisions of Spanish insolvency law and the proper administration of the estate, which under the Insolvency Regulation were quite properly within the exclusive purview of the Spanish courts. However, those issues were concerned with how the competing claims of creditors should be dealt with in the interests of the estate as a whole. The English contractual claims were concerned with whether as a matter of contract there were in fact claims to be asserted in the Spanish insolvency, and if so what those claims were. The court found that there was no conceptual overlap between the two types of action. The risk of conflicting judgments was small, and it was more likely that the Spanish court would find the judgment of the English courts helpful. Accordingly, the court found it would not be expedient to stay the English proceedings.

The court also declined to grant the stays which Marme sought as a matter of discretion. The swaps contracts contained an exclusive English jurisdiction clause, which was a powerful factor suggesting that the English court should assume jurisdiction. In addition, Marme's intention to continue its rescission claim meant that the English courts would in any event have to deal with much of the subject matter.

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### ***Exxonmobil Financial Services Limited v Lehman Brothers International (Europe) Limited [2016] EWHC 2699***

#### **Case summary**

EFMS had entered into tri-party repurchase (TPR) trades with LBIE, the main trading arm of Lehman in London, in the run up to the collapse of the Lehman group. After LBIE entered into administration, EFMS served notice of termination of the outstanding trades which were conducted under the umbrella of a GMRA 2000 master agreement.

Under the GMRA 2000, EFMS as the non-defaulting party was responsible for calculating the net payment due to close out the transactions. As the cash provider/collateral taker under the TPRs, EFMS was due to be repaid the cash sum it had advanced to LBIE, less the value of the collateral portfolio which had been delivered to it by the collateral manager after termination (JPMorgan Chase). As the non-defaulting party, EFMS also had a right under the GMRA 2000 to elect between two valuation methods:

- sale, quotation or valuation: under this mechanism, securities which are sold are to be valued by reference to their net proceeds of sale. If securities have not been sold but quotations have been obtained, they are to be valued at the average of the quotations. If no quotations have been obtained, securities must be valued by the non-defaulting party applying its own methodology
- calculation valuation: under this mechanism, the value of all securities is to be established through calculation by the non-defaulting party applying its own methodology (so sales proceeds and quotations may well be informative but are not binding).

In order to elect for the first of the above mechanisms, the non-defaulting party has to serve a Default Valuation Notice on the defaulting party before the Default Valuation Time, which is defined as being the "close of business in the Appropriate Market on the fifth dealing day after the day on which the Event of Default occurs". EFMS served a notice of termination on

15 September 2008, instructed JPMorgan to sell the collateral portfolio, and served a Default Valuation Notice opting for the first mode of valuation above on 22 September 2008 at around 18:02.

LBIE argued that the Default Valuation Notice was not contractually effective because it had been sent to a LBIE fax number which was not the fax number stipulated in the contract for service of notices, and that in any event it had been served too late because it was received after close of business and was therefore deemed to have been received on 23 September 2008 (after the 5 day deadline for electing for the first mode of valuation had passed).

The judge found that use of the incorrect fax number was a breach of the contractual requirement, but because LBIE had not raised the point at the time, or at any time until disclosure in the proceedings some 6 years later, that it had waived any right to rely on this breach. It should be noted that absent LBIE's tacit acceptance and delay in objecting to receipt on a different fax machine from that stipulated in the contract, the court would otherwise have found that the notice was contractually ineffective. The court also found that 18:02 was not after close of business for banking business in London. Although this finding was heavily caveated as having been reached on limited and somewhat unsatisfactory expert evidence and not intended to have precedent value for other cases, the judge was persuaded to accept EFMS's position that banking business hours carried on until at least 19:00.

On that basis, the court found that the Default Valuation Notice was effective for those securities for which the 18:02BST service time fell before the close of banking business hours in their "most appropriate market" (ie the market in which the bulk of their trading is conducted). For those securities (where sold), the sale prices were to be used for the valuation of those securities.

For the securities with a most appropriate market with a time zone an hour or more ahead of London, the 18:02 service time was held to fall after the 19:00 close of business banking hours. For those securities, and the securities which JPMorgan had been unable to sell at all, the contractual valuation provisions required EFMS to have performed a calculation of their value. EFMS had not in fact done this, because it had believed that its default valuation notice had been served on time and so had relied on sales prices. The issue then was how to establish what value EFMS would have attributed these securities if it had known that it was under a duty to determine a calculated value.

LBIE sought to argue that EFMS was obliged to reach an objectively reasonable valuation standard. This was rejected, and the court held that under now well established principles of English law, the duty which EMFS owed when exercising its contractual discretion to value the securities was to do so honestly, in good faith, and rationally, and without arbitrariness, capriciousness or perversity.

LBIE also sought to attack the valuations which EFMS sought to advance on the basis that they were based on EFMS's expert witnesses' after-the-fact reconstruction of appropriate objective valuations as at the required valuation date. LBIE argued that this was the wrong hypothetical test, and that instead the court should try to determine the hypothetical question of what methodology EFMS would in fact have adopted had it known that it had to value the securities at the relevant time, and then determine what valuations EFMS would have reached on the information then available to it. The court rejected this as too complicated a way to address the issue. The relevant hypothetical was that LBIE would have told EFMS that it was under a

duty to value the relevant securities, at which point EFMS would have valued them in its own commercial interests, which the judge was satisfied fell at the "lower bound level" determined in EFMS's expert evidence.

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## ***Flex-E-Vouchers Ltd v Royal Bank of Scotland (Mercantile Court) (London), 14 September 2016***

### **Case summary**

#### **Facts**

The defendant bank, The Royal Bank of Scotland Plc (RBS), brought an application against the claimant, Flex-E-Vouchers Limited, to strike out a secondary claim in the claimant's particulars of claim which concerned the alleged miss-selling of an interest rate swap.

The claimant operated various gift card schemes, which involved the use of electronic e-money at shopping malls and provided integrated programme management and card transaction services. The swap in this case was obtained by the claimant in the course of its business and was for a term of five years.

The claimant complained that it had been missold this agreement, following which RBS carried out a formal review pursuant to a review procedure entered into between a number of banks at the time and the Financial Services Authority. This review process was monitored and supervised by a skilled person, in this case KPMG. The review concluded that the swap had not complied with agreed standards. However, RBS refused redress on the basis that the claimant would have followed the same course of action in any event.

The primary claim concerned a failure to give advice with reasonable care and skill. The secondary claim concerned a breach of duty in the conduct of the review. The main allegation in this secondary claim was that the swap agreement impliedly incorporated the entire regulatory regime; including the FCA's Principles for Business and COBs, and that the bank was in breach of those regulatory duties. The questions for the court to consider were whether the swap agreement impliedly incorporated the applicable regulations under the regime and whether the implied terms pleaded were obvious and necessary for the effective operation of the contract.

The judge concluded that none of the alleged implied terms could be implied and that there are strict constraints on the implication of terms into a contract. There were three key points to take into account:

- a party who claimed to have been adversely affected by breaches of the FCA's Principles for Business and/or COBs had no right to make a claim for breach of statutory duty as only a private person could claim this
- a complaint could be made to the FCA which had the power to impose sanctions and
- a refusal to imply terms into a swap agreement would not leave misselling victims without a remedy, as they would still have the benefit of the common law.

The court considered various clauses within the contract and held that it would be very unusual for a detailed contract like the instant one to state expressly that the applicable regulations were not incorporated into it - it was not for the bank to explain why there was no implication. In the instant case, there was no room for the implication of terms contended for. Further, the

court held the terms pleaded were not obvious and the contract was commercially coherent without them. The claimant had not articulated why the implication of the terms was necessary.

Additionally, upholding the claimant's secondary claim would cut across the statutory scheme governing the regulatory regime. For these reasons, none of the implied terms could be implied and the secondary claim was struck out.

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## Offshore markets: Guest spot authored and contributed by Appleby

### ***UVW v XYZ (A Registered Agent) (BVI HC (COM) 108 of 2016)***

The Eastern Caribbean Supreme Court has broadened the scope of the jurisdiction to grant Norwich Pharmacal relief in the British Virgin Islands, by holding that it exists in certain circumstances following the delivery of judgment.

The applicant sought disclosure by the registered agent of a BVI company. Its aim was two-fold: to identify assets against which a series of foreign judgments could be enforced, and to secure compliance with the interlocutory freezing orders of a different foreign court.

Wallbank J first rejected the argument that Norwich Pharmacal relief was not available in aid of foreign proceedings. He distinguished the English case of *Regina (Omar) v Secretary of State for Foreign and Commonwealth Affairs* [2013] EWCA Civ 118, in which there was an exclusive procedure for obtaining evidence for use in criminal proceedings abroad. The determinative factor was necessity, and the registered agent had not identified a statutory regime supplying an alternative means of obtaining the information sought. While it was theoretically possible to seek the appointment of a receiver, that was an expensive remedy and Norwich Pharmacal relief was not a last resort; parties should not be put to “complex, costly and potentially nugatory procedures before being accorded” it.

The Judge went on to conclude that Norwich Pharmacal relief is in principle available (1) post-judgment in aid of enforcement where there is a reasonable suspicion that the defendant is mixed up in the wilful evasion of another’s judgment debt, and (2) to assist in securing compliance with domestic or foreign freezing orders. In respect of the former, it was not necessary to identify a specific transaction where the alleged wrongdoer had transferred assets to the BVI corporate vehicle for no reason other than to avoid execution; a general pattern of wilfully evasive conduct was enough. Further, it was not necessary that the company was created for a fraudulent purpose: “if a corporate service provider involves itself in the life or affairs of a company that is, or becomes, used for wrongful purposes, he can expect to be required to give disclosure of information within its possession.”

Wallbank J also confirmed (citing with approval a passage from Hollander on Disclosure) that the Norwich Pharmacal jurisdiction may be used to enable a party to seek “additional documents to plead [a] claim or which will enable him to ascertain whether an action would have reasonable prospects of success”; in other words, what might previously have been characterised as fishing. He accepted that this was a “significant extension of the jurisdiction”, but was confident that “other traditionally accepted checks and balances continue to apply to inform the exercise of the court’s discretion.” These included the need to exercise with care a jurisdiction which invades the privacy of an innocent third party, and consideration of whether other means of obtaining the information were available.

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***Primeo Fund (in liquidation) v Herald Fund SPC (in liquidation) (CICA No 17 of 2015, 19 July 2016, unreported)***

The status of redeeming hedge fund investors was addressed by the Cayman Islands Court of Appeal. The judgment analysed the provisions of section 37(7) of the Companies Law, which deals with the status of redeemable shares and their priority in a liquidation. The Court of Appeal upheld the Grand Court's finding that redemption for the purposes of the section does not include the payment of redemption proceeds. Therefore a member which has filed a valid redemption request and whose shares have been redeemed pursuant to the fund's articles, but who has not been paid redemption proceeds, is not affected by s37(7) but has an independent claim as a creditor under s139(1) of the Companies Law, ranking behind the claims of ordinary creditors. This finding in relation to priority effectively overrules the finding of the Grand Court that shares which have already been redeemed are to be treated as ordinary creditor liabilities ranking alongside, rather than behind, other creditors in the winding up. The Court of Appeal's decision is now being appealed further to the Privy Council, with a request for an expedited hearing to take place early in 2017.

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***Pearson (as Additional Liquidator of Herald Fund SPC (in liquidation)) v Primeo Fund (in liquidation), Grand Court FSD 27 of 2013, Unrep, 2 September 2016***

In the same litigation as the case above, the Cayman Islands Grand Court has issued a further judgment on the power of a liquidator of a solvent Cayman Islands company to rectify the register of members in order to do justice inter se.

The Court had previously found that such a power exists pursuant to s112 of the Companies Law but had not examined the scope of that power or whether it should be exercised in the instant case where the company in liquidation was a feeder fund to a Ponzi scheme and where, as a result, the value of some shareholdings were artificially inflated by fictitious profits. The US Courts have adopted the "net equity" model in such cases to remove the unjust effects of the fraud and the liquidator proposed to do likewise with Herald. Jones J held that such a scenario is a classic case in which that power should be exercised. He further found that this power is a "class remedy" which empowers a liquidator to restore the shareholders of a company to the position they would have been in if a "true NAV" had been available. Since a "true NAV" was not a practical possibility in this case it was held that the next best solution was to treat the initial public offering price of USD1000 or €1000 as the value of each share for the purposes of each subscription or redemption in order to produce similar results to the net equity model favoured by the liquidator. Notably, the Court refused to rectify the shareholding of Primeo which had subscribed for Herald shares in return for its interest in a Madoff managed account – the value of which itself was artificially inflated by fictitious profits.

The Court held that there was no way of rectifying the interests which came about by way of that specific transfer despite recognising the unfairness of the outcome:

"The economic result of this decision is that Primeo will be a major beneficiary, if not the major beneficiary, of Madoff's fraud. As it presently stands, Primeo will succeed in making a recovery in respect of around US\$316m worth of fictitious profits indirectly through its shareholding in Herald. It will do so at the expense of Herald's other shareholders who subscribed cash for their shares because, under the terms of the Settlement Agreement, this amount has to be taken out of Herald's customer claim in the BLMIS bankruptcy."

Perhaps unsurprisingly, this decision is being appealed.

### In the Matter of Up Energy Development Group Limited [2016] SC (Bda) 183

The Supreme Court of Bermuda has clarified the role of provisional liquidators in restructurings by confirming that an insolvent company, in respect of which a creditor's petition has been presented and that wishes to restructure, should not ordinarily be permitted to develop the proposed scheme of arrangement without oversight by provisional liquidators appointed by the Court.

Up Energy was incorporated in Bermuda and listed on the Hong Kong Stock Exchange. The assets of its trading subsidiaries in the PRC included a coal coking facility and three coal mines. These underlying businesses faltered, leading a creditor to issue a statutory demand and, when that was not met, a winding-up petition. At the hearing the creditor sought the appointment of joint provisional liquidators pending the determination of the petition; this was with "soft touch" powers in respect of a restructuring proposal the company had put forward in the meantime. The use of a provisional liquidation in this way is now common in Bermuda (as in other common law jurisdictions), but it was resisted in this case by the company, which argued that it had already appointed restructuring advisers and that a majority of the creditors supported its position.

After a number of adjournments the petitioner renewed its application and the Court agreed that JPLs should indeed be appointed. Chief Justice Kawaley took the opportunity to give a reasoned judgment outlining the governing principles; in doing so he went further than merely confirming the legitimate role of provisional liquidation in insolvent restructurings. There was "a strong starting assumption in favour of the appointment of JPLs, and the burden of displacing that assumption will be [a] heavy one." In his Lordship's view:

"The crucial point is that JPLs play a central role in insolvent restructurings, a role which pivotally shapes the character of the related court proceedings and the role played by this Court. This practice is so deeply entrenched in Bermudian insolvency law practice (and, I suspect, throughout most of the common law world), that all stakeholders have a legitimate expectation that JPLs will be appointed to monitor an insolvent restructuring, if not in all cases, then certainly when a winding-up petition has been presented by a creditor and is still before the Court."

A petitioning creditor need only show a good *prima facie* case for winding up the company. If that is shown, the Court will then consider all relevant circumstances in determining whether to allow the application. Further, in exercising its discretion the Court should not "blindly follow the wishes of the majority of the creditors. In this context at least... democracy does not rule."

One of the concerns raised by the company was that a "soft touch" appointment could be mistaken by those dealing with the company for a "full-blown" provisional liquidation. In his Lordship's view, this could be mitigated by referring in official documents to the Company being "in Provisional Liquidation (for Restructuring Purposes)".

This judgment provides a welcome clarification of the law relevant to Bermudian restructurings, which should lead to greater certainty for both companies and creditors.

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**Sonera Holding B.V. v Cukurova Holding A.S. BVISCMAP 2015/0005 (23 June 2016)**

The Eastern Caribbean Supreme Court has confirmed its jurisdiction to grant an injunction restraining a party from pursuing a foreign arbitration.

In the latest expression of this long-running cross-border dispute, Cukurova successfully argued at first instance that the jurisdiction had been ousted by Section 3(2)(b) of BVI's Arbitration Act 2013, which provided that "the Court shall not interfere in the arbitration of a dispute save as expressly provided in this Act".

But the Court of Appeal disagreed: the power to grant injunctions conferred by Section 24 of the West Indies Associated States Supreme Court (Virgin Islands) Act, which was expressed in the broadest terms, could not be held to have been removed in the absence of clear language. Although Section 3(2)(b) informed the court's approach, a clear distinction had to be drawn between interference with an arbitration and restraining a party from using an arbitral process in a manner abusive of the court's own process.

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**Lime Petroleum Plc & Others CHP 0035/2016 (26 July 2016)**

The Isle of Man's High Court of Justice has concluded that the directors of a company can, at common law, without approval or support from the shareholders, pass a resolution for an insolvent company to be wound up and instruct advocates to file a winding up application on behalf of the company. The result is that the principle in *Re Emmadart* [1979] Ch. 540 – that such a step cannot be taken absent express provision in the articles of association – does not apply in the Isle of Man.

The company sought an order that it be wound up under section 164(1) of the Companies Act 1931 on the grounds that it was unable to pay its debts and on the just and equitable ground on the basis that relations between the shareholders had broken down and there was a deadlock in management.

The proceedings were brought following the passing of a board resolution, but without shareholder approval. Shareholders of the company argued that neither the law nor the articles of association allowed this, relying on the English decisions in *Re Emmadart* and *Re Equiticorp International Plc* (1989) 5 B.C.C. 599.

Deemster Doyle was unpersuaded by the reasoning in *Re Emmadart*, by which he was not bound, and noted that in many jurisdictions it had since been reversed by statute (including England & Wales). It was a company's directors who managed the affairs of a company, including, where necessary, authorising advocates to present applications to the court on the company's behalf. In such cases it was open to a contributory to oppose the application and for the court to come to a conclusion, if one of the statutory grounds were established, whether to wind up the company.

This decision may be contrasted with the recent judgment of the Cayman Islands Grand Court in *Re China Shanshui Cement Group Ltd* [2015(2) CILR 255], in which the principle in *Re Emmadart* was affirmed, notwithstanding an earlier decision of the Grand Court (*Re China Milk Products Group Ltd* [2011(2) CILR 61] in which *Re Emmadart* was not followed).

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## Claims arising from the collapse of Providence and Lumiere

The recent demise of Providence Global Ltd in Guernsey and the related independent financial adviser Lumiere Wealth Ltd in Jersey has generated much interest in the Channel Islands and elsewhere.

Lumiere is jointly owned by Providence Global (65%) and Christopher Byrne (35%). Providence Global is a holding company for a number of other companies, including various investment funds and two factoring companies in Brazil. Funds invested in the investment funds were lent to the factoring businesses. By June 2016, Lumiere clients had invested approximately £14m in one of the investment funds. Lumiere staff had also invested in the Group. Some of the group's entities were regulated by the Guernsey Financial Services Commission; others were not. Lumiere was licensed by the Jersey Financial Services Commission from 16 April 2015 as a Class D Investment Business (allowing it to advise on investments but not to hold client assets).

One of the ultimate beneficial owners of the Providence group is Mr Antonio Buzaneli, who also part-owns Providence companies based in the US. Funds from US investors total approximately \$64m, and were also invested in the same factoring businesses in Brazil.

It appears however that of the funds invested in the Guernsey funds, only a small proportion was invested in the factoring businesses. The rest was diverted to other parts of the Providence group and other companies owned by Mr Buzaneli.

In June, the Jersey Financial Services Commission directed that Lumiere could no longer offer investment advice in relation to the Providence funds. There followed an investigation into the alleged regulatory failings at Lumiere, including the suitability of investment advice provided to its clients.

The funds in Guernsey were suspended in July.

At the beginning of August this year, the US branch in Miami filed for US bankruptcy protection after the Securities and Exchange Commission took steps to close its operations. There followed urgent applications to the Guernsey Royal Court by the Guernsey Financial Services Commission, and then an application to the Jersey Royal Court, prompted by the resignation of all the directors of two of the Guernsey investment funds.

In Guernsey, Deloitte were appointed as Administration Managers under Protection of Investors legislation. Liquidators were also appointed in relation to the Providence parent company. The parent company was discovered to be insolvent, and a winding up process was initiated.

The Administrator's report was delivered in September, in which it was confirmed that investors' funds were not fully accountable. The Guernsey Financial Services Commission stated that it was working with the Jersey Financial Services Commission and the US Securities and Exchange Commission and law enforcement agencies.

In Minnesota, a Court has issued an order requiring Mr Buzaneli to surrender his passports and he is prohibited from leaving the US until further order. Mr Buzaneli's assets are frozen, and he is ordered to "repatriate" all his assets to the US. Meanwhile in Jersey, Mr Christopher Byrne was arrested on 7 October.

Further developments in relation to this interesting case are awaited.

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## About RPC

RPC is a modern, progressive and commercially focused City law firm. We have 83 partners and over 600 employees based in London, Hong Kong, Singapore and Bristol.



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- Winner – Law Firm of the Year – The British Legal Awards 2015
- Winner – Competition and Regulatory Team of the Year – The British Legal Awards 2015
- Winner – Law Firm of the Year – The Lawyer Awards 2014
- Winner – Law Firm of the Year – Halsbury Legal Awards 2014
- Winner – Commercial Team of the Year – The British Legal Awards 2014
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