RPC

Financial Litigation roundup

Spring 2015

Welcome to the latest edition of our Financial Litigation roundup. In this edition, we consider recent judgments and ongoing cases from the banking and financial world in the UK and Asia, as well as regulatory developments across those jurisdictions.

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English Judgments

SPL Private Finance (PF1) IC Limited and others v Arch Financial Products LLP and others; SPL Private Finance (PF2) IC Ltd and other v Robin Farrell[1]

Summary: The High Court clarifies the position regarding liability of investment managers, applying established legal principles of agency and inducement.

Arch Financial Products (Arch FP) was the investment manager of the Arch-Cru funds, which constituted 22 Guernsey incorporated cell companies (Cells). Each of the Cells held their own assets and had their own particular investment objectives.

Arch FP entered into identical investment management agreements (IMAs) with each of the Cells. Among other terms, the IMAs provided that Arch FP would take reasonable care in the day-to-day management of the Cells.

A claim against Arch FP and its CEO Mr Robin Farrell was subsequently brought by 18 of the 22 Cells. It was alleged that £20m of investments made by Arch FP on their behalf in a student housing business known as "Club Easy" was driven by its own interest in obtaining illegitimate payments, in the form of £6m of fees, rather than proper consideration of the investment's merits.

The court held that no reasonable investment manager could possibly have considered that the investment in Club Easy was in the best interests of the Cells. The court set out the following principles which applied to a fund manager when exercising discretionary management powers:

1. in the absence of any contractual term to the contrary, the investment manager owes to its clients a duty to exercise discretionary powers with due care and skill. The necessary degree of care requires a risk/reward analysis
2. an investment manager that undertakes to act for its clients in circumstances giving rise to a relationship of trust and confidence owes to them a duty of loyalty. The obligation is two-fold: avoiding conflicts (or potential conflicts) of interest; and not to profit from its position
3. a "disclosure" defence will only succeed where a fund manager can demonstrate that before entering into a transaction it made full disclosure of material facts and the extent of its own interests.

Following the decision in *South Australian Asset Management Co. v York Montague*[2] the Cells were awarded damages of over £22m, as their funds were used for a type of investment to which they should never have been committed (thus entitling them to recover the entire loss).

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McWilliam v Norton Finance (UK) Ltd (in liquidation)[3]

Summary: A credit broker was in a fiduciary relationship with borrowers and breached this duty when it failed to inform them of the amount of commission received from lenders and PPI providers.

In 2006 Mr and Mrs McWilliams (McWilliams) obtained a consumer loan from Norton Finance UK Limited (Norton) of £25,500. Including a PPI premium of £3,745 (funded as part of the loan), a broker fee of £750 and a completion fee of £500, the total amount borrowed amounted to

1. [2014] EWHC 4268 (Comm).
2. [1977] AC 191.
3. [2015] EWCA Civ 186.

£30,495. What the McWilliams were not aware of was that Norton had received commissions from the lenders of 8.77% of the loan (£2,675) and from the PPI providers of 45% of the premium (£1,685.25), totalling £4,360.25.

The McWilliams brought a claim against Norton seeking repayment of the allegedly secret commissions and claiming breach of fiduciary duty. At first instance, Norton had initially conceded it had received the commissions, but later withdrew the admission by stating they had in fact been received by a third party, Fintel Limited (Fintel). The court found that since no commissions had been received by Norton, no fiduciary duty was owed.

The McWilliams appealed and three issues arose for consideration:

1. whether the court was right to allow Norton to withdraw its admission
2. if not, whether Norton owed the McWilliams fiduciary duties
3. if such a duty was owed, whether it was breached.

The Court of Appeal viewed the withdrawal of the admission as one of "manifest unfairness". It referred to CPR PD14 and the considerations under paragraph 7.2, namely that it prejudiced the McWilliams' case. Accordingly, it proceeded to consider issues 2 and 3 on the basis that commissions were taken by Norton.

Despite the lack of a contractual agreement between Norton and the McWilliams, the court found that there was a contract of agency. Norton as agent owed a fiduciary duty to the McWilliams, since the latter were "vulnerable people of relatively modest means with a history of credit problems" and reposed trust and confidence in Norton in relation to the transaction.

The Court of Appeal held that Norton should not have placed itself in a position where its duty and interest conflicted, nor could it profit from its position without the McWilliams' informed consent. It was irrelevant that the service was non-advisory, since this did not affect the parties' relationship.

Although Norton had informed the McWilliams of commission being received from the lenders (both in the application form and in the borrower information guide), it had not informed them of the actual quantum of the commission. The Court of Appeal held that knowledge of the size of the commission payments was necessary in order to "bring home" the potential conflict on the part of the brokers.

It follows that the borrowers' informed consent had not been given and the commission sums received by Norton were ordered to be paid to the McWilliams, together with interest.

The Financial Conduct Authority (FCA) implemented new rules on 2 January 2015 with respect to consumer credit regulation, namely that commissions must be disclosed by credit brokers. However, the amount need not be disclosed unless asked for. This case moves in the direction of a greater level of protection for consumers, seeing as it requires the disclosure of the amount of the commission by the brokers, irrespective of whether this had been asked for by their customers.

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Tael One Partners Limited v Morgan Stanley & Co International PLC[4]

Summary: "Payment premium" under loan documented under the Loan Market Association standard terms and conditions.

Tael One Partners Limited (Tael) was a lender under a syndicated loan (Loan) and in January 2010 sold part of it ($11m out of the total $32m) to Morgan Stanley & Co International PLC (Morgan Stanley), under the LMA Standard Terms and Conditions for par trading (LMA Terms).

The terms of the Loan required the borrowers to pay the lenders interest on the principal sum and a fee upon early payment of the loan (Payment Premium). In December 2010 the borrowers eventually prepaid the Loan in full and paid the Payment Premium to the then lenders only.

Tael argued that the Payment Premium was part of the consideration for the Loan and because it was calculated by reference to the period the Loan was outstanding, it should therefore be treated as a payment "expressed to accrue by reference to the lapse of time" under condition 11.9 of the LMA terms. Under the LMA terms payments "expressed to accrue by reference to the lapse of time" were apportioned between the buyer and seller according to the length of time each of them had held the loan.

The trial judge agreed with Tael's arguments. The Court of Appeal, however, reversed the decision. Tael appealed to the Supreme Court.

The Supreme Court unanimously dismissed Tael's appeal. It held that the Payment Premium was not "expressed to accrue by reference to the lapse of time" but instead "accrues on a defined event" ie date of prepayment. As the Payment Premium had not accrued at the time Tael sold the Loan to Morgan Stanley, it did not fall within condition 11.9 and therefore Tael was not entitled to any part of it.

The decision is consistent with the general practice in the loan trading market, where loans are sold and on-sold and it is unlikely that there is any intention to create continuing payment rights and obligations.

The case reinforces the need to be cautious when using standard forms of contract, in particular in the secondary loan trade market. It is noteworthy not only for those operating in the loan market but also those involved in the drafting and interpretation of these contracts.

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Myers and another v Kestrel Acquisitions Ltd (Kestrel) and others[5]

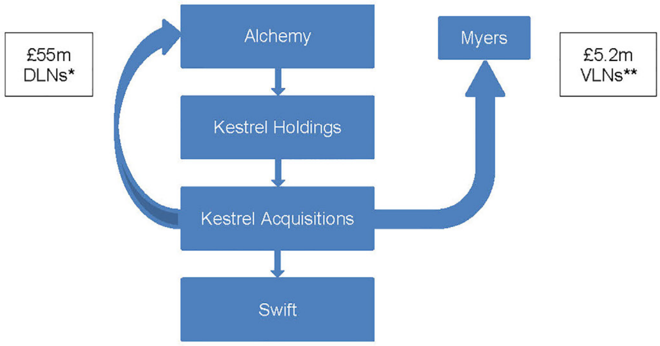
Summary: The High Court was unwilling to imply an obligation that any modifications made by majority noteholders should be in good faith for the benefit of the entire class.

Mr and Mrs Myers (Myers), had sold their shares in Swift Advances (Swift), a mortgage and consumer credit lending company, to private equity firm Alchemy Partners (Alchemy) in 2004, for £90m. The consideration was structured as follows: £4.6m in cash; £75m in guaranteed loan notes; £74,000 in shares; £5.2m vendor loan notes at 12% pa (VLNs); and £5m if Swift was sold within 12 months.

4. [2015] UKSC 12 (11 March 2015).
5. [2015] EWHC 916 (Ch).

In order to fund the consideration for the shares in Swift, Kestrel Acquisitions (Kestrel Acquisitions) issued £55m in Discounted Loan Notes (DLNs) to Alchemy. Swift became a subsidiary of Kestrel Acquisitions, an SPV, which in turn issued the VLNs as part of the consideration for Swift.

Post-Sale Structure



*£55m "Discounted Loan Notes" which were issued by Kestrel Acquisitions to Alchemy.
**£5.2m "Vendor Loan Notes" which were issued to the Myers by Kestrel Acquisitions.

A key term of the VLNs was that Kestrel Acquisitions was entitled to "make any modification" to the VLNs if sanctioned by a resolution of the VLN holders, or unilaterally if the modification was consistent with amendments to the DLNs. Another key term was an event of default provision stipulating that if "any Group Company" was unable to pay its debts within the meaning of section 123 of the Insolvency Act 1986, the VLNs would become immediately redeemable.

Since the VLNs had been issued, a number of amendments had been made which deferred the redemption date (this was initially scheduled for 2010, but was eventually deferred until 2018). Additionally, the VLNs were subordinated to various other "follow-on" loan notes (the FONs) which were issued between 2007 and 2009. These were subject to interest at 25% compounded, and as of 2013, further deferrals of the redemption date had aggravated the exponential rate at which interest was accruing. The Myers believed that there was no prospect of Kestrel trading out of these issues, and as such no prospect of repayment.

The Myers sought declarations under CPR Part 8 that:

1. the changes made to the VLNs were not "modifications"
2. modifications must be made in good faith; and
3. Kestrel Acquisitions and Kestrel Holdings were insolvent.

Modification

The Myers argued that "modification" implied the preservation of essential characteristics of loan notes. An essential characteristic of a loan note is the obligation to pay. By extending the redemption and subordinating the loan notes, the Myers' rights had been extinguished and thus the VLNs were no longer "loans". The defendants on the other hand argued that the parties expressly provided for extensive modification and so both the variations and subordinations of the loan must have been envisaged.

The court held that the changes to the date of repayment of the notes and their subordination to the FONs fell within the express powers of modification conferred by the terms of the VLNs, and therefore there was no "extinction of rights of the scale and nature" as considered in *Mercantile Investment and General Trust Co v International Company of Mexico*[6].

Implied term of good faith

The Myers argued it is trite law the majority may not vary the rights of a minority other than in good faith and for the benefit of the class. The counter-argument by the defendants was that there was no general duty of good faith in commercial dealings, and in any case this was an arms-length commercial transaction where both sides were legally represented.

The court accepted that there was no general duty of good faith in commercial contracts but that such a duty could be implied on the facts. However, on the facts it rejected the implied duty based largely on the grounds that the VLNs and DLNs were a single class for all purposes and therefore there was no requirement for the majority (the DLN noteholders) to act bona fide in the interests of the VLN noteholders when exercising their powers under the DLNs.

Insolvency

The court rejected the defendants' argument that the power to modify and restructure the loan notes, free of any requirement of good faith, meant that the company was, in practical terms, solvent. Instead, it held that the rights of the majority to impose variations on the minority did not go so far as to allow a writing down of the nominal value of the notes. This in turn meant that Kestrel Acquisitions and Kestrel Holdings were in fact both insolvent for the purposes of section 123 of the Insolvency Act 1986. On their terms, the VLNs were therefore immediately repayable.

The case shows that there remains considerable judicial resistance to imposing a general duty of good faith, particularly in commercial transactions. The courts seem content for the principle of good faith to develop on a piecemeal basis in English law. However, it is clear from *Myers* that such a duty is unlikely to be implied where express terms have been freely negotiated, in extensive and detailed documentation, by sophisticated and adequately represented parties.

Settlement was reached between the parties before the judgment was handed down, and no appeal will therefore be forthcoming. It remains to be seen whether *Myers* will be followed, but it appears this would require compelling facts.

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Fondazione Enasarco v (1) Lehman Brothers Finance S.A. and (2) Antharcite Rated Investments (Cayman) Limited[7]

Summary: A non-defaulting party to the termination of a transaction under an ISDA Master Agreement had validly calculated its loss by using the price of a subsequent replacement transaction.

In 2007, Fondazione Enasarco (Enasarco) invested in €780m principal protected notes (Notes), issued by Antharcite Rated Investments (Cayman) Limited (ARIC), an offshore special purpose vehicle. A cash-settled put option was granted by Lehman Brothers Finance (LBF), and this was documented under the 1992 ISDA Master Agreement (Master Agreement).

6. [1893] 1 Ch 484].
7. [2015] EWHC 1307.

The collapse of the Lehman Brothers Group in 2008 caused LBF to file for bankruptcy protection on 15 September 2008 (Early Termination Date), and subsequently default under the Master Agreement.

Due to pressure from the authorities and the media in Italy, Enasarco sought to take immediate steps to obtain replacement capital protection. On 6 May 2009, Enasarco executed a replacement transaction with Credit Suisse. A number of terms were different from those in the original option (Replacement Transaction).

The Master Agreement provided for calculation of a payment upon early termination. Accordingly, on 16 September 2009, ARIC as the non-defaulting party used the price for the Replacement Transaction as the basis for its calculation of loss and determined that $61,507,902 was due to it from LBF.

LBF challenged ARIC's calculation on three main points, namely:

1. 6 May 2009 was not the earliest reasonably practicable date after the Early Termination Date as of which ARIC could have determined its loss on the basis of a quotation for a replacement transaction
2. the terms of the Replacement Transaction were so different from those of the original transaction that the price of the Replacement Transaction could not be used to determine ARIC's loss; and
3. the date of the calculation statement (16 September 2009), was not "as soon as reasonably practicable following the occurrence" of the Early Termination Date.

The court found that the calculation of ARIC's loss had been reasonable and in good faith in accordance with the terms of the Master Agreement.

Following the test set out in *Associated Provincial Picture House Ltd v Wednesbury Corporation*[8], the judge held that the party determining the loss is not required to comply with an objective standard of care, but must not arrive at a determination which "no reasonable non-defaulting party could come to" (para 53).

Given the uncertainty of the market following the collapse of Lehman Brothers Group, Enasarco had done the best it could to find the Replacement Transaction and the quotation date of 6 May 2009 was not unreasonable. It was more appropriate to look to prices actually quoted for a transaction (albeit some eight months later) than any hypothetical prices (para 49).

The fact that the terms of the Replacement Transaction were not identical to those of the original transaction did not prevent it from being a comparable replacement for the purposes of calculating loss.

Finally, the court accepted that the calculation statement could have been provided earlier than September 2009. However, this did not impact on the validity or binding nature of the calculation of loss (para 139).

This case is a helpful guide to the court's interpretation of the close-out provisions in the ISDA Master Agreement. Participants in the structured products and derivatives markets should bear in mind the following points:

8. [1948] 1 KB 233.

1. a party wishing to challenge a calculation of loss determined by the non-defaulting party must show that the latter acted in an irrational, Wednesbury, manner
2. calculation of loss as at a date several months after the Early Termination Date, will be accepted provided it is shown the non-defaulting party took all reasonable steps it could amidst the complexity of a volatile situation
3. even if the terms of two transactions differ slightly, a quotation from a leading dealer is still stronger evidence and more reliable than the use of a hypothetical financial model.

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Ongoing Cases

Guardian Care Homes v Lloyds Banking Group

Lloyds Banking Group (Lloyds) faces a new battle with a care home operator relating to the mis-selling of interest rate swaps in the wake of the LIBOR manipulation scandal.

This is the second claim Guardian Care Homes (Guardian) has brought against Lloyds. The first was settled in 2011. Guardian now claims the 2011 settlement is void on the basis that Lloyds has since been found to be one of the many banks which conspired to manipulate LIBOR. In a claim filed on 7 April 2015, Guardian stated "In making LIBOR representations, Lloyds gave, and was in breach of, an implied warranty in relation to each of the swaps and the 2011 settlement agreement that the Libor representations were true".

The claim follows Guardian's action against Barclays Bank, which was settled in 2014 for a reported £40m weeks before trial.

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RBS – GRG Business Action Group

Around 270 small and medium sized companies have united under the RBS-GRG Business Action Group to bring a claim against Royal Bank of Scotland's Global Restructuring Group, alleging unlawful means conspiracy against the bank and four individuals in relation to the way in which assets were acquired by the bank from businesses in financial distress.

The bank was previously under scrutiny following claims of mis-selling government-backed loans to small businesses, which also complained of being incorrectly informed about the amount of loan repayments.

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Regulatory investigations and developments

Seven new benchmarks are now regulated by the FCA

Following the scandal in 2011 surrounding LIBOR, the Financial Conduct Authority (FCA) decided to regulate activities in the benchmarks arena. Two specified activities were introduced via an amending order to the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO). Since 2 April 2013 it has been a specified activity to:

1. provide information in relation to a specified benchmark; and
2. administer a specified benchmark.

These activities were extended to seven further benchmarks by way of a further amendment to RAO which came into force on 1 April 2015. Seven benchmarks are now subject to FCA regulation:

1. Sterling Overnight Index Average (SONIA)
2. Repurchase Overnight Index Average (RONIA)
3. ISDAFIX (soon to be renamed the ICE Swap Rate)
4. WM/Reuters (WMR) London 4pm Closing Spot Rate
5. London Gold Fixing (soon to be replaced by the LBMA Gold Price)
6. LBMA Silver Price
7. ICE Brent Index.

The fact that the FCA took regulatory action suggests that these benchmarks were, at the very least, susceptible to manipulation.

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The European Commission fines ICAP for facilitating Yen interest rate derivatives cartels

In February 2015, the European Commission announced that it had fined ICAP (a UK-based broker) a total of €14.96m for having breached EU competition laws, in particular for having facilitated several cartels in the yen interest rate derivatives sector.

The fine follows a cartel settlement decision in December 2013, in which five banks and one interdealer broker had settled the Commission's investigation into their participation in the infringements for a combined sum of €669.7m.

ICAP had refused to settle their case with the Commission in December 2013, which resulted in the Commission continuing with their investigation.

Investigation

Interest rate derivatives, such as swaps, future and options, are used to manage the risk of interest rate fluctuations. The value of these contracts is often linked to benchmark interest rates such as LIBOR, including Japanese yen (JPY), pound sterling, US dollar, euro and Swiss franc. Anticompetitive behaviour in relation to such benchmarks might affect the value of contracts linked to the benchmark.

The Commission's investigation centred around the following anticompetitive conduct:

1. discussions between traders at participating banks regarding their JPY LIBOR submissions; and
2. the exchange of commercially sensitive information on trading positions or future JPY LIBOR submissions.

For its part, the Commission found that ICAP had facilitated six out of seven cartels, in particular by: (i) disseminating misleading information to certain panel banks; (ii) using its contacts at several JPY LIBOR panel banks that did not participate in the infringements to seek to influence their JPY LIBOR submissions; and (iii) acting as a conduit between traders of particular banks, thereby facilitating the anticompetitive conduct.

Ongoing enforcement

In announcing the fines against ICAP, the Commission has stated that it will continue its efforts to detect and punish similar anticompetitive practices. This includes not only regulatory action, but also continuing to focus on efforts to promote private damages actions against those firms which engage in anticompetitive conduct. This risk applies equally to settling and non-settling parties.

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FCA to launch market study for investment and corporate banking

Following its wholesale review into the financial sector, the FCA has announced plans to launch a market study into the investment and corporate banking sector. The study will enable the FCA to examine whether competition is working well and help it to assess whether further intervention or remedies will be required.

It is currently expected that the FCA will announce the precise terms of reference in May 2015, but while the precise scope of the market study has yet to be confirmed, the FCA has identified that it has concerns about the following aspects of the market:

1. limited transparency over both price and quality may make it difficult for clients to assess value for money; and
2. bundling and cross-selling of services may make it difficult for new entrants to compete and may contribute to low levels of transparency.

In selecting the investment and corporate banking sector for in-depth scrutiny, the FCA has pointed to the sector's size and importance to the UK economy and is clearly mindful of the importance of ensuring effective competition in the market.

The market study, which is due to commence in spring 2015, could run for around two years, depending on whether the FCA proceeds pursuant to its powers under the Enterprise Act, or those under the FSMA regime. In either case, the study is likely to impose considerable time and cost on market participants.

Separately, the FCA may also, at a later stage, undertake a market study to examine whether purchasers get value for money when buying asset management services. This has yet to be confirmed.

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Hong Kong

DBS Bank (Hong Kong) Ltd v Sit Pan Jit[9]

In the latest mis-selling claim in Hong Kong, the Court of First Instance has maintained an approach consistent with other recent cases, rejecting an investor's claim based upon misrepresentation and suggesting that the principle of contractual estoppel is alive and well.

Mr Sit was a private client of DBS who utilised credit facilities provided by DBS to invest in investment products, including a series of Equity Linked Notes (ELNs). These were structured products, the performance of which was linked to the value of certain underlying equities. The contractual documents stated that DBS provided an "execution only service" and contained the usual terms upon which a bank agrees to provide such a service; namely, that Mr Sit declared that – (1) he had not relied upon any representations that the Bank had made regarding suitability; (2) he had exercised his own independent judgment before making a decision to enter into the investment; (3) he was aware that he was investing on a margin basis, the terms of which he understood; and (4) he understood the nature, features and risks involved in investing in ELNs.

With the onset of the financial crisis in 2008, the value of the ELNs declined significantly. Following a failure by Mr Sit to meet a margin call, DBS exercised its right to sell a number of investments and apply the proceeds to reduce his indebtedness. DBS then demanded that Mr Sit settle the balance and sued him for payment. Mr Sit counterclaimed that the ELN had been mis-sold to him, alleging: (i) the existence of an oral agreement with DBS which contained terms that DBS' relationship manager would be personally responsible for looking after Mr Sit's investments and would not make risky investments on his behalf; (ii) a series of misrepresentations which induced him to purchase the ELNs; and (iii) breach of implied duties of care in contract and tort, together with a parallel fiduciary duty which DBS owed him, by recommending investment products which were not suitable and failing to explain the nature, mechanism and risk involved in investing in those products.

The Court rejected Mr Sit's defence and counterclaim in its entirety. It found the existence of the alleged oral contract not to be believable and held that the terms which governed the relationship between Mr Sit and DBS were set out in the contractual documents. DBS had, therefore, contracted with Mr Sit to provide an execution only service. The court rejected Mr Sit's case on misrepresentation, finding that he was an experienced businessman and a relatively sophisticated investor who knew he was trading on margin and understood the risks of doing so. He also understood the key features/risks of the ELN and that they were not "principal protected". In this regard, the existence of recordings and transcripts of conversations between DBS and Mr Sit was crucial.

On the basis of these findings of fact, it was not necessary for DBS to rely upon contractual estoppel; namely, the contractual provisions confirming that the bank was not providing advice and that the customer could not rely on any representations made. However, the court considered that Mr Sit was estopped from bringing any claim based upon the alleged misrepresentations or from asserting that he had not understood the basis upon which the credit facilities were provided to him or that he was trading on margin. He was also estopped from arguing that he had not made his own, independent, investment decisions in relation to the ELN or that he had not understood the risk involved in investing in these products.

9. HCA No. 382 of 2009.

The court also rejected Mr Sit's argument that the relevant terms of the Banking Documents were subject to the provisions of Control of Exemption Clauses Ordinance (Cap. 71) and Misrepresentation Ordinance (Cap. 284) and should be struck out as unreasonable on the basis that the relevant clauses defined the limited scope of the services that DBS had contracted to provide (in contrast to exclusion clauses).

Having determined that Mr Sit had contracted with DBS on an execution only basis under the express terms of the contractual documents, there was no scope for the court to imply any terms which imposed an advisory duty or to find that there had been any voluntary assumption of responsibility. The claims in contract, tort and for breach of fiduciary duty inevitably failed.

The prevailing approach remains that the Hong Kong courts will be slow to interfere with the principle that written commercial contracts, the terms of which are clear and which have been signed by the parties, are intended to mean what they say. This is particularly so where the claimant who alleges mis-selling is a relatively sophisticated investor, with access to whatever independent advice he or she may require before entering into an agreement with a bank to provide credit or investment facilities or before entering into any specific investment decision.

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Investors' claims – investments with "best friend" advisers

As noted in the Spring 2014 roundup, professional investors in Hong Kong have had a challenging time pursuing claims against banks and financial advisers[10].

That said, investors do succeed in the Hong Kong courts. However, they tend to be retail or less sophisticated investors[11]. A recent case is *Kurtzman v Petter*[12]. This case demonstrates that friends who profess to have a financial acumen and who undertake investments for one another but fail to exercise appropriate skill and care can be found to owe a fiduciary duty.

While the decision in *Kurtzman v Petter* turns on its facts, it is not an usual scenario in a city where many profess to have financial acumen and experience and do make investments on behalf of family and friends. The case is clearly a warning that such investments can come with financial responsibilities to the investor.

In *Kurtzman v Petter*, the plaintiff investor was a professional man but not a sophisticated investor. Looking for extra yield in the fallout from the 2008 financial crisis, he invested not insignificant amounts of money with a then "best friend" (the defendant), who professed to have investing experience and acumen. The investments were apparently made in the defendant's name and enabled the plaintiff to access certain wealth management products otherwise not available to him.

Towards the end of 2010 the plaintiff wanted his money back, but it was locked up. After various delays, the plaintiff eventually sued the defendant for the balance he claimed was owing to him. His claim succeeded on the basis of breach of fiduciary duty and as a claim for money had by the defendant for the plaintiff's use. The fiduciary duty was held to arise out of the relationship between the two men and the ascendancy or influence of the one over the other; the breach being (among other things) a failure to exercise proper skill or care and to return the funds on time.

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10. For example, see footnotes 12-18 of Financial Litigation roundup, Spring 2014. Also see – *DBS Bank (Hong Kong) Ltd v Sit Pan Jit*, HCA No. 382 of 2009, 2 April 2015; another failed investor's mis-selling claim.
11. *Field v Barber Asia Ltd* [2004] 3 HKLRD 871.
12. HCA No. 38 of 2012, 6 March 2015.

Winding up order imposed on China Metal Recycling

On 26 February 2015, the SFC obtained an unprecedented order of the Court of First Instance for the winding up of China Metal Recycling (China Metal) under Section 212 of Hong Kong's Securities and Futures Ordinance (the SFO). The winding up order demonstrates the SFC's determination to pursue and combat corporate misconduct and seek to enforce against fraudulent activity.

Section 212 SFO allows the SFC to bring winding up proceedings under Hong Kong's Companies Ordinance if it can show that the winding up of a company is just and equitable, and in the public interest to do so. This order represents the first of its kind to be obtained by the SFC under section 212.

The SFC presented its petition to wind up China Metal in July 2013 and obtained an order to appoint provisional liquidators for the company. The petition followed the suspension of trading in China Metal's shares, first imposed by the Stock Exchange of Hong Kong (the SEHK) in late January 2013.

The SFC successfully demonstrated that the affairs of China Metal Recycling involved a highly complex, sophisticated and dishonest scheme spanning Hong Kong, Macao, the Mainland and the US. The scheme inflated China Metal Recycling's performance, revenue and profit dating back to the time of its IPO prospectus in 2009 and becoming larger and more complex in the subsequent years until it was brought to an end by the SFC. The scheme involved the use of China Metal's wholly owned off-shore subsidiary in Macao which was the conduit for a substantial part of the company's annual profits between 2007 and 2012 and was also a factory for generating false documents and instruments by which these profits were falsified. It also involved fake shipments of scrap metal between the US and the Mainland, false shipping documents, false accounts, and highly complex "round robin" transactions spanning continents.

The majority of most of China Metals' significant assets are located in the Mainland and the extent to which the SFC will be able to enforce its order is not yet fully clear. However, on the basis that the SFC worked closely with the China Securities Regulatory Commission in the investigation, the two regulators may continue to cooperate regarding enforcement.

While the SFC clearly means to push its regulatory agenda and continue to be one of the most proactive and innovative regulators among those in major international financial centres, it is likely that the power to bring winding up petitions will be reserved for use where the more standard measures may not have had (or may not be considered capable of having) an adequate deterrent effect.

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Update on SFC's consultation on client agreements

The Securities and Futures Commission (SFC) in Hong Kong is due to report shortly on its further consultation on the client agreements requirements for persons or entities licensed by or registered with the SFC.

The SFC's Code of Conduct will be amended to include provision that intermediaries' client agreements must include a contractual term to the effect that the agreements do not contain terms that are inconsistent with their obligations under the Code of Conduct nor inaccurately describe their services. These new provisions will come into effect once the SFC concludes its consultation on the incorporation of a new "suitability term" for client agreements. That consultation period closed on 24 December 2014 and the SFC's further deliberations are awaited[13].

In the meantime, as anticipated the SFC has issued a Circular to licensed intermediaries giving guidance in the form of responses to FAQs on: (i) corporate professional investor assessment (Appendix 1 of the Circular – effective as from 25 March 2016); and (ii) description of services in client agreements (Appendix 2 of the Circular – clarification of existing requirements)[14].

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Market misconduct proceedings against short selling author of research report

The SFC continues its pursuit of alleged market wrongdoers and, in doing so, is living up to its reputation as the most aggressive market regulator in Asia.

In its press release of 19 March 2015, the SFC announced that the Market Misconduct Tribunal (MMT) had fixed hearing dates between February and March 2016, with respect to the SFC's complaint of alleged market misconduct against the head of Citron Research, a US based trading and research company.

Citron Research published a research report on Evergrande Real Estate Group Limited, a Chinese company listed on the Stock Exchange of Hong Kong. The report stated, among other things, that Evergrande was insolvent and had consistently presented fraudulent information to the investing public. The share price of Evergrande fell sharply immediately following the publication of the report. The SFC alleges that shortly before publishing the report, Citron short sold 4.1 m shares of Evergrande making a profit of approximately $1.7 m. The SFC's Notice commencing the MMT proceedings is publicly available[15].

These proceedings are also noteworthy because (as far as we are aware) they are the first time that the SFC has pursued a case of market misconduct arising out of alleged short-selling with respect to shares listed in Hong Kong.

The SFC's action comes on the back of the now infamous "Tiger Asia Management" (Tiger Asia) market misconduct proceedings, which culminated in dealing bans ("cold shoulder" and "cease and desist" orders) in October 2014 and restorative compensation orders in December 2013, against Tiger Asia and one or more of its former senior officers[16]. In its press release concerning Tiger Asia, the SFC's Executive Director of Enforcement is quoted as stating that:

"The SFC will track down and take action against wrongdoers wherever in the world they may lurk"[17].

This is a sign of things to come and heralds a sterner approach to market misconduct of shares listed in Hong Kong, be the alleged market participants in Hong Kong or overseas.

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13. For more on this issue, see our Financial Services Blogs, dated 3 October 2014 and 9 February 2015 – www.rpc.co.uk/media centre/blogs.
14. See – http://www.sfc.hk/edistributionWeb/gateway/EN/circular/doc?refNo=15EC4.
15. www.mmt.gov.hk (see – "Rulings/Notices). There is no allegation that the company has done anything wrong.
16. www.mmt.gov.hk (see – "Reports – Bank of China and China Construction Bank Corporation").
17. SFC Press Release 9 October 2014. Also see our Financial Services Blog, dated 10 October 2014 – www.rpc.co.uk/media centre/blogs.

Singapore

Singapore International Commercial Court

The Singapore International Commercial Court (SICC) was launched with much fanfare in January of this year. As its name suggests, the SICC has been set up to determine claims that are "international" and "commercial" in nature and where the parties have agreed to a jurisdiction clause that gives the SICC jurisdiction.

The SICC is a division of the High Court and its proceedings are governed by the same rules of court[18]. The SICC is presided over by a panel of international judges.

It will be interesting to see if other jurisdictions in Asia follow suit and whether Singapore enjoys a "first mover" advantage in this regard. While the SICC serves to supplement Singapore's reputation as an international disputes resolution centre, alongside the Singapore International Arbitration Centre (SIAC) and Singapore International Mediation Centre, parties will need to consider the relative merits of commercial arbitration – eg, (i) Singapore is a signatory to the New York Convention and SIAC arbitral awards are enforceable in other convention states[19]; and (ii) in its 2010 rules, the SIAC introduced an expedited procedure which requires awards to be issued within six months of a tribunal being appointed (designed to address delay with respect to unmeritorious arbitration proceedings).

Comparisons are often made between Singapore and Hong Kong. While both compete as international disputes resolution centres, it is worth noting that Singapore is a city state while Hong Kong is a Special Administrative Region of China (within "one country, two systems"). There could be local sensitivities in some quarters in having an "International" court set-up in Hong Kong SAR. That said, since the late 1960s, as part of its High Court, Hong Kong has had its own "Commercial List" for heavyweight commercial disputes (modelled on the Commercial Court in London)[20]. Both jurisdictions also are active in promoting their much respected international arbitration centres and mediation services (or "med-arb")[21].

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18. Singapore Rules of Court O.110. The court rules provide for what is meant by "international" and "commercial" and are similar to the use of those words in Singapore international arbitrations.
19. Convention on the Recognition and Enforcement of Foreign Arbitral Awards. The enforceability of SICC judgments overseas compared to arbitration awards remains to be seen.
20. Rules of High Court of Hong Kong, Order 72; and Practice Direction SL1.1 ("Commercial List"), including a new pilot scheme for e-discovery (SL1.2).
21. For example, see Johnathan Cary & Robert Rhoda on "*Arbitration Rising*", IFLR (Capital Markets) April 2015.

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