BANKING DISPUTES

QUARTERLY

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DLA Piper's Banking & Finance Litigation team welcomes you to our quarterly round-up, designed to keep you informed of the latest news and legal developments, and to let you know about future developments that may affect your practice.

ON THE HORIZON

RECENT DEVELOPMENTS & CASES

SPOTLIGHT ON...

CONTACTS

ON THE HORIZON

In this section we summarise cases, legislation and other developments in prospect in coming months:

- **Exercise of discretion: meaning of "commercially reasonable manner"**

"Consent not to be unreasonably withheld" clauses are common in finance transactions but what precisely do the words mean and by what standards will a party be judged when exercising its discretion?

The Court of Appeal will be looking at this issue towards the end of February 2014 when it hears an appeal in the case of *Barclays Bank Plc v (1) Unicredit Bank AG and (2) Unicredit Bank Austria AG* [2012] EWHC 3655 (Comm). The issue under the microscope will be whether Barclays exercised its discretion in a "commercially reasonable manner" when it refused to consent to the early termination of a number of finance transactions.

In December 2012 the High Court ruled that the exercise of discretion under these clauses should be judged by an objective standard of reasonableness, not by whether the party makes its decision honestly and in good faith and not arbitrarily, capriciously or irrationally. The court held that Barclays had acted in a commercially reasonable manner, that Barclays was entitled to act in its own commercial interests and that it did not have to take account of the interests of Unicredit unless the costs to Unicredit would be so disproportionate that no reasonable financier in Barclays' position could have reached such a decision.

This case is the first which deals with the issue of reasonableness of consent specifically in the context of finance transactions. Given the prevalence of "consent not to be unreasonably withheld" clauses in facility agreements and other finance documents the outcome of the appeal will be awaited with interest.

- **Tightening the regulatory regime for Claims Management Companies**

The Ministry of Justice has announced tough new measures to crack down on the bad practices of rogue Claims Management Companies (CMCs).

The Claims Management Regulation Unit is to be expanded and strengthened and will be given new powers to impose financial penalties on CMCs which do not comply with their conduct rules or otherwise breach their conditions of authorisation. There will be a full public consultation regarding the detail of the necessary changes to facilitate a Claims Management Regulation Financial Penalty Scheme in early 2014.

The government is also consulting on tougher conduct rules which will impose duties on CMCs to ensure that claims they submit have a realistic chance of success and are supported by full evidence. The proposed reforms are designed to help free up banks to deal with legitimate claims more quickly and to deter CMCs from pursuing speculative claims and using unsolicited calls and texts to gather information.

- **JP Morgan Chase Bank & Anor v Berliner Verkehrsbetriebe (BVG) Anstalt des Öffentlichen Rechts**

  The trial of an important CDO dispute between JP Morgan and Berlin's public transport provider, BVG, has started in the Commercial Court in London and is scheduled to last 10 weeks.

  The case concerns a complex credit default swap arrangement which was intended to provide protection to BVG against risks inherent in cross-border leasing arrangements. Part of the transaction involved a swap agreement pursuant to which BVG sold to JP Morgan protection worth US$200 million against the credit risk of 150 companies in return for a premium of US$7 million. As a result of the turmoil in the financial markets in 2008 some of those credit risks materialised, giving rise to JP Morgan's US$112 million claim.

  JPMorgan seeks declarations about the validity of the agreement but also advances a monetary claim. BVG argues it had incorrect advice from the bank. The trial will examine events leading up to the swap, the meaning and effect of the swap, BVG's understanding of the swap, the extent to which BVG misunderstood the swap, and the extent to which any misunderstanding was the result of what was said or not said by JP Morgan. Importantly it will also involve a consideration of whether the swap is invalid because it is ultra vires.

  The case is one of the first concerning derivatives concluded by a European public body to get to trial. Its outcome could influence dozens of lawsuits over losses on swap agreements between banks and local governments/community-owned utilities in the UK, Germany and Italy.

RECENT DEVELOPMENTS & CASES

In this section, we take a more in-depth look at some the cases and other developments affecting the banking and financial industry in recent weeks.

Dahabshiil Transfer Services Ltd v Barclays Bank Plc; Harada Limited and another v Barclays Bank Plc

By Paul Smith (Legal Director) and Amy Billing (Associate), London

In November 2013 the Chancery Division granted an interim injunction to restrain Barclays from withdrawing its services to three claimants carrying on "money service businesses", until a trial of their substantive claims to be held later in 2014.

Background

The Money Laundering Regulations 2007 (SI 2007 No. 2157, Reg. 2(1)) define a money service business as:

> *"an undertaking which by way of business operates a currency exchange office, transmits money (or any representations of monetary value) by any means or cashes cheques which are made payable to customers."*

The money service business market is considered a high risk sector, open to manipulation by money-launderers and financers of terrorism. In view of such risks, the increasing regulatory requirements imposed upon banks operating in this area, and the imposition of fines on banks for failing to maintain adequate anti-money laundering measures, Barclays made a policy decision to reduce its involvement and exposure to this sector. It served notice upon a number of its money service business customers of its intention to terminate their banking services. Among those affected were the three claimants, who applied for injunctions to prevent Barclays from withdrawing their banking services in view of the impact that this would have on their businesses.

The claim brought by Dahabshiil generated particular publicity, since Dahabshiil has substantial operations in Somalia, where there is no formal banking system and money can only be transferred to individuals through money service businesses such as Dahabshiil. The market's concerns about criminal and terrorist activities in Somalia are therefore to be balanced against the potential impact on the Somali economy and ordinary Somalis of actions which could seriously affect Dahabshiil's ability to carry on its operations.

Whilst there was no dispute that Barclays was contractually entitled to terminate its provision of services to each of the claimants, the claimants sought injunctions to prevent Barclays from doing so on the basis that Barclays held a dominant position in the market for the provision of banking services to money transfer businesses, and that by withdrawing services without objective justification Barclays would be abusing its dominant position contrary to Article 102 of the Treaty on the Functioning of the European Union and the Chapter II prohibition in the Competition Act 1998.

A serious issue to be tried?

Hearing the applications, Mr Justice Henderson made it clear that this was not a breach of contract case and that, if it were, there would be no triable issue as a matter of contract, stating that:

> *"There is no dispute that Barclays is contractually entitled to terminate its provision of banking services to each of the claimants. Like any other private business, Barclays is entitled to choose its customers. Although heavily regulated in the public interest, banks are under no public law duty to make their services available to particular categories of customer."*

The success of the claimants' applications therefore depended on the competition law issues. In order to succeed it was necessary for the claimants to demonstrate that there was a serious issue to be tried as to whether Barclays held a dominant position in the markets in which the claimants operated.

Mr Justice Henderson was persuaded that there were indeed serious issues to be tried. He reached his decision on the basis of expert and other evidence submitted by the claimants suggesting that Barclays enjoyed a high market share in the particular markets relevant to each claimant. For the market sector relevant to Dahabshiil, evidence was advanced suggesting that Barclays provided banking services to around 70% of that market (potentially even more, given the withdrawal of other banks from the market). This was said to be strong prima-facie evidence of a dominant position from a competition law perspective, although that market share figure and conclusion is contested by Barclays. Barclays also contested the claims on the basis that its conduct in withdrawing banking services from money service businesses was objectively justified and proportionate in the circumstances. Again, the judge found that this should be examined at a full trial.

Having considered the balance of convenience between Barclays and the claimants, and whether damages after the fact would be an adequate remedy for the claimants in the event that the injunctions were not granted, Mr Justice Henderson concluded that the interim injunctions should be ordered. He found that there was a greater danger of irremediable prejudice to the claimants if injunctions were refused than there was to Barclays in maintaining the status quo pending a full trial.

Implications

The Dahabshiil judgment serves as a helpful reminder of the principles the court will apply when deciding whether or not to grant an interim injunction, which Mr Justice Henderson reaffirmed to be those set out in *American Cyanamid Co (No. 1) v Ethicon Limited* [1975] AC 396. These principals were lucidly summarised in the more recent Privy Council opinion in *National Commercial Bank Jamaica Limited v Olint Corpn Ltd* UKPC 16 [2009], where Lord Hoffman observed (at paragraphs 16 and 17):

> *"It is often said that the purpose of an interlocutory injunction is to preserve the status quo, but it is of course impossible to stop the world pending trial. The court may order a defendant to do something or not to do something else, but such restrictions on the defendant's freedom of action will have consequences, for him and for others, which a court has to take into account. The purpose of such an injunction is to improve the chances of the court being able to do justice after a determination of the merits at the trial. At the interlocutory stage, the court must therefore assess whether granting or withholding an injunction is more likely to produce a just result... that means that if damages will be an adequate remedy for the plaintiff, there are no grounds for interference with the defendant's freedom of action by the grant of an injunction. Likewise, if there is a serious issue to be tried and the plaintiff could be prejudiced by the acts or omissions of the defendant pending trial and the cross-undertaking in damages would provide the defendant with an adequate remedy if it turns out that his freedom of action should not have been restrained, then an injunction should ordinarily be granted... The basic principle is that the court should take whichever course seems likely to cause the least irremediable prejudice to one party or the other."*

The Dahabshiil judgment is also an illustration of how the traditional contractual basis for the relationship between a bank and its customers is these days subject to ever-increasing regulation and may be affected by a host of other legal factors including competition law issues. Here, a bank's contractual ability to withdraw its services from a customer, particularly in niche market areas where the bank may have a larger, dominant position, is potentially circumscribed by competition legislation – even though the bank may be able to point to objective reasons for its decision and has followed a proper process. It is however important to remember that this was only an interim application and the case remains to be determined at full trial later this year.

Goldman Sachs -v- Videocon Global: Mastering precision

By Jeremy Andrews (Partner) and Oliver Felton (Associate), London. This article first appeared in the December 2013 issue of Butterworths' Journal of International Banking and Financial Law.

The High Court has provided useful guidance on the effect of successive margin call notices, and the need for precision in statements of loss in the context of the 1992 (Multicurrency – Cross Border) ISDA Master Agreement where the parties have chosen "Loss" and "Second Method" under that form.

On 20 September 2013, the Commercial Court gave judgment in favour of Goldman Sachs International ("**Bank**"), against Videocon Global Limited and Videocon Industries (together, "**Videocon**") regarding two currency option transactions ("**Transactions**") between the parties. The Transactions were contracted pursuant to the 1992 (Multicurrency – Cross Border) ISDA Master Agreement, with a Schedule specifying "Loss" and "Second Method" (the "**ISDA Master**").

Having entered into the Transactions, on 23 November 2011 the Bank made a margin call of Videocon for US$840,000. Subsequently, between 24 and 28 November 2011 the Bank made three further margin calls. None of the margin calls were met. Videocon did instruct its bank to make payment of US$840,000 to the Bank (in respect of the first margin call), but cancelled that instruction on 2 December 2011.

The Bank delivered to Videocon a Notice of Potential Event of Default dated 28 November 2011, based on a failure to meet the first margin call, and then a notice designating an early termination date as "*2 December 2011, or, if this notice is not effective on such date, the next Local Business Day on which the notice is effective* " ("**Early Termination Notice**"). On 14 December 2011, the Bank delivered to Videocon a statement of loss under Section 6(d) of the ISDA Master. Videocon failed to pay and the Bank therefore sued Videocon for its losses attributable to (i) Videocon's failure to meet the margin calls; and (ii) early termination of the Transactions.

In its defence, Videocon argued that:

- the Early Termination Notice was invalid because the first margin call had been superseded by the subsequent three margin calls that the Bank had made (rendering the Early Termination Notice meaningless);
- as Videocon had instructed its bank to make payment in respect of the first margin call, it had tendered performance of payment, which the Bank had refused to receive;
- "*the next Local Business Day*" specified in the Early Termination Notice was not precise enough to comply with the requirements under Section 6(a) of the ISDA Master.

In relation to those arguments, the Court found:

- the first margin call remained effective notwithstanding the later margin calls;
- there was no tender of performance by Videocon and no refusal by the Bank to receive payment. On the facts, Videocon had cancelled the payment instructions it had given;
- it was sufficient for the purposes of Section 6(a) of the ISDA Master that the Early Termination Notice specified a day or "*the next Local Business Day*" as the day on which it was effective.

Accordingly, the Court awarded summary judgment on liability in the Bank's favour.

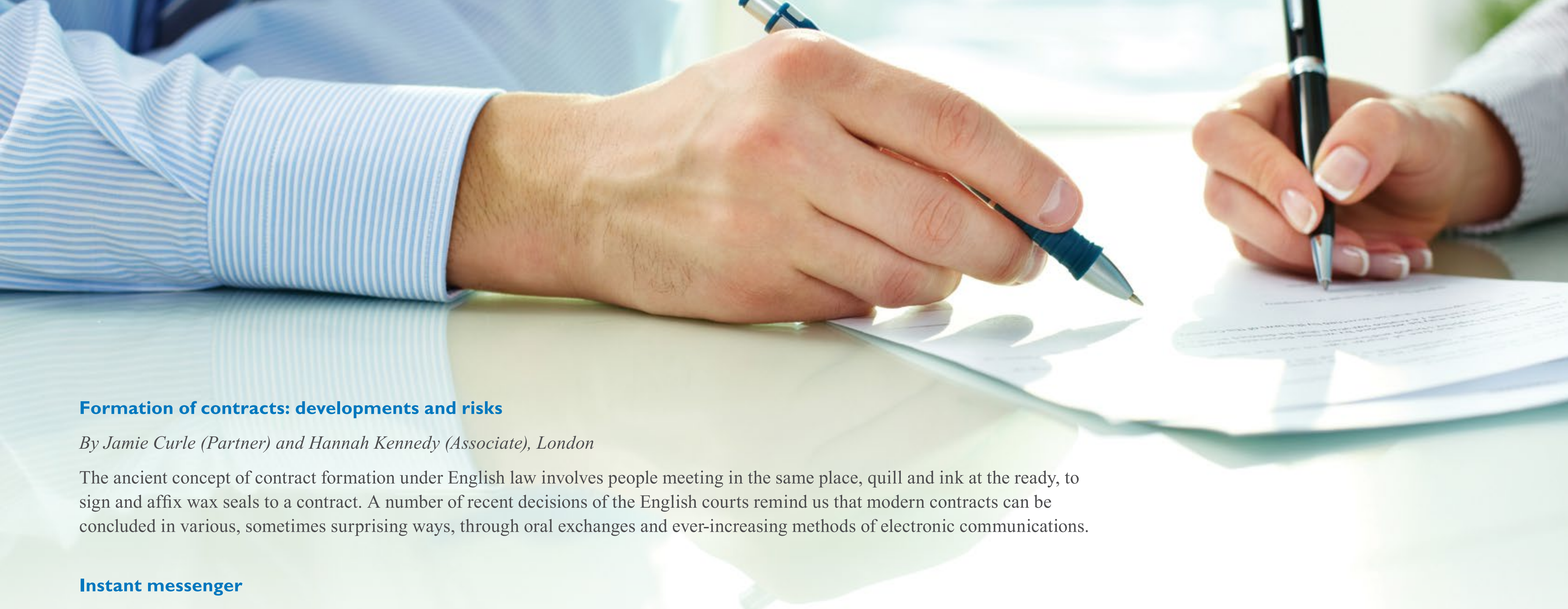
However, the Court's judgment did not extend to the quantum of the Bank's claim. This was because the Bank's statement of loss sent to Videocon had failed to meet the requirements of the ISDA Master.

In its statement of loss, the Bank specified two sums in respect of each of the Transactions, which were said to be based on an independent quote from a third party source and a quote from a Goldman Sachs entity, for spot exchange rates, forward rates and FX volatilities. The sums were said to be calculated using an options pricing model based on market accepted standards. The Court held that the statement of loss was not detailed enough to comply with Section 6(d) of the ISDA Master Agreement. In particular, it did not:

- set out its calculations in reasonable detail;
- adequately identify the sources from which the quotes were obtained, nor detail the quotes themselves;
- explain the particular pricing model said to be relied upon.

Accordingly, the quantum of the Bank's losses would be determined at trial.

The decision is a useful reminder of the need for banks to be sufficiently precise in their notice of termination and statement of loss when terminating a transaction pursuant to the 1992 (Multicurrency – Cross Border) form of ISDA Master, where the parties have chosen "Loss" and "Second Method" under that form. In particular, the judge held that part of the purpose of the agreed requirements of the statement of loss in those circumstances was that it should provide the receiving party information sufficient "*to enable a reasonable understanding of how the figures stated were arrived at.....* [to] *assist the party.... to form a view..... as to whether the determination of Loss satisfied the contractual requirements of reasonableness and good faith*". Banks can also be reassured that successive margin calls will not supersede earlier calls as they are made.



Formation of contracts: developments and risks

By Jamie Curle (Partner) and Hannah Kennedy (Associate), London

The ancient concept of contract formation under English law involves people meeting in the same place, quill and ink at the ready, to sign and affix wax seals to a contract. A number of recent decisions of the English courts remind us that modern contracts can be concluded in various, sometimes surprising ways, through oral exchanges and ever-increasing methods of electronic communications.

Instant messenger

In the recent case of *BNP Paribas v Anchorage Capital Europe* [2013] EWHC 3073 (Comm) it was recognised, albeit at an interim stage, that instant communicator messages are capable of giving rise to a legally binding contract.

The case concerns subordinated private placement notes issued by Anglo Irish Bank (AIB). In October 2012 these were purchased by BNP Paribas, with a view to selling them on to the defendants, part of the Anchorage group. BNP Paribas negotiated a sale with the Anchorage entities over an instant messaging communicator. Two purchases were apparently negotiated, but there was some delay in completing the transaction, during which AIB went into special liquidation rendering the notes worthless.

BNP Paribas brought a claim in the English High Court, arguing that a valid binding contract had been concluded over the instant messenger system and that Anchorage owed them the purchase price. The Anchorage entities brought parallel proceedings in New York with a view to establishing that no such contract existed. Whether the contract was capable of being concluded over instant messenger was of key importance not only to whether Anchorage was liable to pay the purchase price, but also to the question of whether the English or New York courts had jurisdiction to hear the claim.

In the English High Court, Males J decided that there was indeed a good arguable case that the instant messages had led to the creation of a valid contract, which was sufficient to establish the jurisdiction of the English Court. The judge referred to various factors indicating the existence of a contract, and noted that the language used in the instant messages was that of a binding contract. There was no suggestion that further negotiations were to take place, and Anchorage had taken steps to hedge one set of notes, which only made sense if the parties were proceeding on the basis that a contract had been or would be concluded, and the parties' conduct suggested a mutual understanding that a contract had been concluded.

Whilst this was only a preliminary decision on jurisdiction, and the case will proceed to a full hearing, it is nevertheless an interesting illustration that the High Court is prepared to accept that a multi-million dollar contract is capable of being made, informally, over an instant messenger system. As a result of decisions such as this, as well as related issues arising from ill-advised instant communication messages coming to light during regulatory investigations, a number of banks and financial institutions have started to ban the use of instant messaging systems by their employees for work-related communication.

Incomplete terms

In another recent case, *Proton Energy Group SA v Orien Lieutuva* [2013] EWHC 2872 (Comm), the English Commercial Court found that a contract had been concluded even though certain terms were still stated to be subject to further negotiation.

This case concerned negotiations for the sale and purchase of 25,000 tonnes of crude oil. Various terms had been agreed, which the claimant confirmed by email to the defendant purchaser, making what it described as a "*firm offer*" to sell. Subsequent emails that day concluded with the claimant emailing the defendant confirming the price and indicating that all outstanding terms would be *"discussed and mutually agreed"* through negotiations. The defendant replied, simply, *"Confirmed"*.

Shortly thereafter, the claimant sent a detailed draft contract to the defendant, the terms of which led to further email exchanges, with all of the claimant's e-mails being headed *"We are pleased to confirm our sale"*. Eventually negotiations broke down, with at least one issue still to be agreed. The claimant argued that the defendant was in repudiatory breach of the contract which had been concluded on the terms of the draft, and sought to accept the repudiation and seek damages for breach of contract. The defendant argued that the contract had not yet come into existence, and relied on the outstanding terms to be agreed in support of this.

His Honour Judge Mackie QC disagreed with the defendant, calling the contract a "classic spot deal" and observing that the nature of the market in crude oil is such that principal terms are often agreed quickly, with details to be refined later. The language used by the parties was "that of commitment", and the subsequent negotiation of the details did not detract from this. It was therefore held that a binding contract had indeed been formed, and that the defendant was in breach.

Two places at once

In *Conductive Inkjet Technology Ltd v Uni-Pixel Displays Inc* [2013] EWHC 2968 (Ch), it was held that it is possible in principle for a contract to have been created in two places at once, raising potential issues over the applicable governing law and jurisdiction.

Usually, a contract is formed in the place where acceptance of the offer is communicated to the offeror. For instantaneous forms of communication, such as email, the contract is formed in the place where the acceptance is received. In a previous case in 2004, *Apple Corps Ltd v Apple Computer Inc* [2004] EWHC 768 (Ch) the English High Court had already opened the possibility of a contract being formed in two places at once, in the case of a contract concluded over the telephone, in circumstances where the parties had deliberately avoided choosing a jurisdiction clause because they could not agree on one. Mann J in that case stated, albeit *obiter*, that it was *"arguably a much more satisfying analysis to say that the contract was made in both places at the same time"*.

The *Conductive Inkjet* case concerned contracts concluded via email between parties in England and the US relating to the use of certain IP rights. These facts were, according to Roth J, analogous to those in *Apple Corps*, since the parties deliberately left out any choice of law or jurisdiction clause. The claimant brought proceedings in England, claiming that the defendant had breached confidentiality obligations, and seeking damages, declarations and a range of injunctions. The defendants disputed jurisdiction, and issued their own proceedings in Texas. The English High Court therefore had to determine jurisdiction as a preliminary issue.

In relation to one of the contracts in issue, the parties had concluded the contract via email whilst located in England and Texas, and had sent each other signed copies of the executed agreement. The claimant argued that jurisdiction could be established in respect of this contract because it had been made in England. The judge found that it would be *"wholly artificial"* to apply traditional contractual rules to determine where the contract had been made, and that it would especially be *"arbitrary to do so on the basis of the order in which a document was signed"*. Accordingly, for the purposes of establishing jurisdiction, there was a good arguable case that the contract had been made in *both* England and Texas.

It is not clear whether subsequent courts will follow this reasoning or revert to the traditional rule that the contract is made where the email confirming agreement to a contract is received. Arguably, the decision is to be welcomed as allowing an attractive degree of flexibility in international business relations; on the other hand, decisions such as this can be said to create uncertainty over the law that may govern the parties' contract and the courts that may have jurisdiction to hear any disputes arising.

Conclusion

English law has shown itself flexible and modern enough to recognise that modern business practises mean there is no reason why contracts should not be concluded through new media, such as forms of instant communication, leaving some terms to be agreed, or that contracts may be concluded in two places at once. This flexibility is one of English law's attractions and a strong factor in favour of choosing English law as the governing law of agreements. That said, parties must take care and be aware of the various circumstances in which a contract may be concluded, perhaps before the parties expect it to take effect, and before they have fully considered the implications of the terms that may (or may not) have been agreed upon.

SPOTLIGHT ON...

OUR BANKING LITIGATION PRACTICE IN NEW YORK

Within the US, the banking sector continues to be the subject of intense regulatory attention and substantial civil litigation in the wake of the financial crisis. Our lawyers represent financial institutions, banking regulators and individuals who work in the financial services industry in actions pending in courts throughout the US. We also represent companies and individuals in proceedings initiated by the US Department of Justice and various state criminal authorities, by the Securities Exchange Commission, the Commodity Futures Trading Commission and other agencies, and by FINRA and other self-regulatory organizations in the securities industry. In addition, we conduct internal investigations for clients to identify potential issues before litigation or enforcement proceedings have begun.

Our US banking litigation team represents banking institutions ranging from community banks to multinational organisations in consumer class actions, lending disputes and similar commercial litigation. In addition, we have represented clients in a wide array of matters arising from the financial crisis and its aftermath, and we do so frequently in collaboration with our colleagues in other jurisdictions.

The financial crisis gave rise to substantial disputes concerning the underwriting, securitisation, sale and management of residential mortgage loans and disputes concerning interest rate swaps and other derivative products. Our US litigators have represented clients in regulatory proceedings, in class actions under the federal securities laws, in bankruptcy litigation and in other civil proceedings in all of these areas. Currently, we are preparing for trial in the defence of a fixed income trader who is facing criminal charges initiated by the Office of the Special Inspector General for the Troubled Asset Relief Program (SIG-TARP) relating to transactions in mortgage backed securities. We have also represented several clients in litigation arising from the collapse of Bernard L. Madoff Securities and other Ponzi schemes that were revealed as a result of the financial crisis. In addition, we have represented the US deposit insurance agency, the Federal Deposit Insurance Corporation (FDIC), as receiver for failed banks in litigation with holding companies and their investors in courts around the US. Our frequent work with the FDIC has given us additional insight into the enforcement of capital and liquidity standards and other issues of importance to US banking regulators.

For participants in US financial markets, wherever they may be based, the intersection of competition law and the financial markets is likely to be a subject of significant US enforcement and civil litigation activity for many years to come. Our US litigation team has represented clients in connection with recent investigations into alleged collusion in the establishment of market benchmarks, including LIBOR, EURIBOR and ISDA rates, and in connection with an industry investigation into alleged collusion among inter-dealer brokers in the market for credit-default swaps.

For further information about our US banking litigation practice, please contact Richard Hans or John Clarke.

CONTACTS

Jean-Pierre Douglas-Henry
Partner
T +44 20 7153 7373
jp.douglashenry@dlapiper.com

Hugh Evans
Partner
T +44 113 369 220
hughevans@dlapiper.com

Ben Johnson
Partner
T +44 161 235 4536
ben.johnson@dlapiper.com

Jamie Curle
Partner
T +44 20 7796 6396
jamie.curle@dlapiper.com

Adam Ibrahim
Partner
T +44 113 369 2216
adam.ibrahim@dlapiper.com

Ioannis Alexopoulos
Partner
T +44 20 7796 6897
ioannis.alexopoulos@dlapiper.com

Jeremy Andrews
partner
T +44 20 7796 6280
jeremy.andrews@dlapiper.com

Stewart Plant
Partner
T +44 161 235 4544
stewart.plant@dlapiper.com

Paul Smith
Legal Director
T +44 20 7796 6489
paul.m.smith@dlapiper.com

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