TRAVERS SMITH

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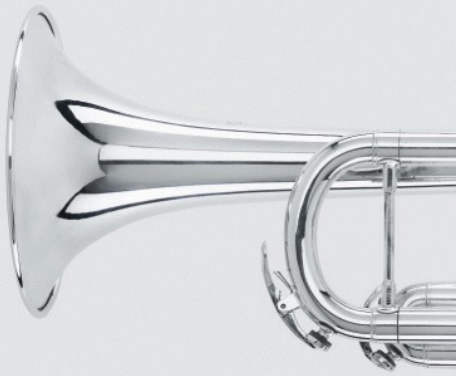

Welcome to the monthly finance bulletin from our banking and corporate recovery department. This issue contains our usual overview of some recent market developments and trends in the finance sector, including a spotlight on Crowdfunding or "P2P". Please get in touch if it raises any issues that you would like to discuss.

Jeremy Walsh, Head of Banking and Corporate Recovery Department

LIBOR Manipulation and Swap mis-selling

On 8 November, the Court of Appeal resolved conflicting decisions at first instance, in a decision unlikely to be welcomed by banks party to interest rate swaps or other products linked to a LIBOR determination. In *Graiseley Properties v Barclays Bank [2013]* the claimant applied to amend its particulars of claim in relation to an interest rate swap mis-selling case to include an allegation that Barclays had made implied representations with respect to the accuracy of LIBOR. That application was successful, but in *Deutsche Bank AG v Unitech [2013*], a similar application failed before Cooke J. The Court of Appeal heard both claims at the same time and, preferring Flaux J's judgment in *Graiseley* (otherwise known as the Guardian Homes Case) allowed both amendments to claim to go ahead. The Court of Appeal concluded that the implied representation plea was at least arguable. Whilst acknowledging that both Barclays' and Deutsche Bank's counter-arguments were also persuasive, the Court of Appeal elected not to exclude claims which the parties wished to advance, concluding that it was appropriate for a trial judge to have the opportunity to consider the merits of the argument. In that context, much may depend on whether the absence of discussion about the integrity of the LIBOR rate during the sales process is compatible with a representation having been made, and, if it has, the effect of contractual exculpatory wording. The awareness of senior management at the banks with respect to LIBOR manipulation, if established, might be held to be sufficient to negate any such exculpatory wording.

LMA Super Senior and Super Senior/HYB Intercreditor

On 12 November, LMA added (a) a Super Senior Multicurrency Revolving Facility Agreement; and (b) a Super Senior Intercreditor Agreement to their suite of leveraged finance documents.

Each of the documents are accompanied by User Guides. The Super Senior Revolver is for use in conjunction with a High Yield Bond/Senior Secured Note Facility otherwise structured as a leveraged deal. The documents envisage equity investment, loan note and/or preference share investments and under the Intercreditor Agreement, the Revolving Lenders, Hedging providers and bondholders under the High Yield Bond are ranked *pari passu*.

ESMA/EMIR: Reporting Start Date

In August 2013, ESMA, the EMIR regulator, requested a twelve month delay to the scheduled start date of 12 February 2014 for reporting exchange traded derivatives to trade repositories. Article 9 of EMIR requires all counterparties and central counterparties to report all derivative trades to a registered trade repository.

On 7 November, the same day on which ESMA approved the registration of the first four trade repositories (the US Depository Trust and Clearing Corporation's Derivatives Repository; Poland's Central Securities Depository; REGIS-TR; and the LSE's Una Vista) under EMIR, the European Commission wrote to ESMA rejecting any possibility of delay, citing the absolute necessity of spotting the build-up of destabilising risks and identifying counterparties' exposure. ESMA has, in a further letter dated 14 November to the European Commission's Director General for internal market and services, again emphasised that the guidance necessary to achieve precise reporting requirements is far from formulated, potentially leading to the generation of useless data.

Piercing the Veil

The principle, established since 1897, that a company has separate legal personality from its shareholders has been subject to considerable analysis by the English senior courts this year, notably in the Supreme Court decisions of *Prest v Petrodel Resources Ltd [2013]* and *VTB Capital Plc v Nutritek International Corp [2013]*. Unfortunately, neither case introduces crystal clarity to the circumstances in which the courts are entitled to look through companies to fix liability on the persons controlling those companies.

Spotlight on…P2P/Crowdfunding: FCA Consults

Crowdfunding or "Peer to Peer" (P2P) lending is a way of raising equity or finance by seeking small amounts from large numbers of people over the internet. "BrewDog", an Aberdeen brewery has recently raised £7m via investments in shares in its "Equity for Punks" crowdfunding scheme and is to be closely followed by the Arran Brewery. Some websites offer a platform for a number of fund-raisers (Crowdcube.com hosts over 400 businesses and Seedrs.com about 300) whilst former user Nicola Horlick is proposing to establish a site of her own. The disintermediation of banks has also proceeded apace and in volume in the USA, where earlier this month US$53m of P2P loans were securitised by Eaglewood Capital, ironically to institutional investors. The crowdfunding sites have attracted the scrutiny of the FCA, which on 24 October published a bulky consultation paper (CP13/13) in advance of the adoption of its consumer credit role in April 2014. The paper makes it clear that arranging the sale of unlisted equity or debt securities already constitutes the regulated activity of arranging deals in specified investments. The FCA intends to impose further controls on such investment-based platforms from 1 October 2014, including restricting the class of permitted retail clients to sophisticated or high net worth individuals; or those "restricted" investors which certify that no more than 10% of their portfolio is invested in unlisted securities; or those investors which confirm that they have been independently advised by an authorised person.

Loan-based crowdfunding platforms, currently unregulated, are perceived by the FCA to constitute a lower risk, but with effect from 1 April 2014 it is proposed that these will be designated investment businesses and as such subject to the COBs rules for designated investments with respect to disclosure rules. Firms establishing loan-based crowdfunding platforms will also be subject to further controls including minimum capital requirements; the segregation of client money in compliance with CASS; dispute resolution rules; provisions ensuring the continuity of service on platform failure and reporting rights. The permitted retail client rules referred to above and applicable to investment-based platforms will not apply to loan-based platforms, but the rules on appropriateness will apply to ensure that investors are restricted to those understanding the risks involved. Finally, the cancellation opportunities afforded to retail investors by the Distance Marketing Directive which are applicable to loan-based platforms are not easily accommodated following the disbursement of a loan, and the FCA has proposed the possibility of the cancellation period commencing on investor registration with the platform, rather than on actual investment.

In *VTB v Nutritek*, the Supreme Court acknowledged that there were circumstances in which this veil can be pierced where a company is used as mere cloak to conceal wrongdoing. In this case, however, the claimants sought to argue that the submission by a company to the jurisdiction of the English courts implied a similar submission by the individual who controlled that company and the Supreme Court was not happy to extend an exception to the overarching principle (usually applied in circumstances where it was sought to make a company liable for the obligations of the controlling shareholder) to a situation where the controlling shareholder of a company was to be treated as a co-contracting party with such company. Whilst the Supreme Court emphasised its reluctance to expand the doctrine of piercing the corporate veil, it failed to precisely identify the circumstances in which the doctrine would apply. Another opportunity was afforded by the divorce case, *Prest*, in which the central argument was whether the assets of offshore companies owned by the husband should properly be distinguished from his own assets. The Supreme Court was able to sidestep this opportunity, reaching their decision in favour of the wife on the basis of the husband's entitlement to the corporate assets by means of his beneficial ownership through a resulting trust. The Supreme Court was prepared to agree with the Court of Appeal that an opportunity to pierce the corporate veil would be afforded where a person controls a company which is being used to avoid personal liability for some wrongdoing, but this argument was not made out in this case, where no evidence was presented to establish that the offshore companies had been used to avoid liability to his wife, rather than simply to achieve tax avoidance goals. Lord Sumption's formulation in *Prest* (which the other Lordships thought too narrow) was that a fraudulent purpose would unravel a corporate structure – where a company is used as a camouflage to conceal the identity of individuals or where a company structure is used to evade a legal obligation or restriction, or its enforcement. Further observations of Lord Sumption, however, suggest that the courts should use these "concealment" or "evasion" exceptions only as a last resort, where no other remedies against the controlling person are available. Such other remedies might encompass the use of resulting trusts, as in *Prest*, or the characterisation of a controlling shareholder as a "shadow director" where, for instance, a company's assets have been depleted by transfer to another (*Vivendi v Murray Richards [2013]*). As the law currently stands, the only principles that might be safely distilled from these Supreme Court decisions is that the corporate veil will be pierced only in exceptional circumstances and as a rarely used tool "to undo wrongdoing ... when no other principle is available".

Public Register of Beneficial Share Ownership

On 31 October, BIS announced that, pursuant to proposals made at the G8 Conference in June, a central register will be established identifying the *beneficial* owners of more than 25% of the shares in a UK company and that the register is to be made accessible to the public.

In the courts

Kavanagh & Others v Crystal Palace FC Ltd and another [2013] EWCA Civ 1410

Under Regulation 7 (1) of the TUPE Regulations 2006, if an employee is dismissed by virtue of a prospective transfer or a reason connected with a transfer, that dismissal will be unfair unless the reason is an economic, technical or organisational (ETO) reason. In *Spaceright Europe Limited v Baillavoine [2011]*, the Court of Appeal held that a dismissal could be for a reason connected with the transfer even where the transferee was not known at the time of dismissal, and that for the ETO defence to apply, the dismissal needed to be connected to the viable continuation of the business, rather than simply achieving a sale. The administrators of Crystal Palace FC anticipated the eventual sale of the club, but in the meantime decided that cash flow problems could be alleviated by dismissing Mrs Kavanagh and three other employees. At first instance, the Tribunal decided that the dismissals were for an ETO reason – at the date of dismissal, the sale of the Club was only a possibility and the overriding requirement was to reduce the wages bill. On appeal, the decision was reversed, the Employment Appeals Tribunal (EAT) citing the *Spaceright* decision, the administrators' aim to sell the business and the fact that the redundancies made the ultimate sale of the Club more likely. The Court of Appeal reversed the EAT finding and reinstated the original Tribunal decision that the dismissals were justified on an ETO basis.

The Court of Appeal reasoned that the application of Regulation 7 (1) of TUPE was "an intensely fact-sensitive process" and that the present facts were significantly different from those in *Spaceright*. The liquidation of a football club would result in the exodus of its principal assets (its players) leaving few assets to be realised for the benefit of creditors. Accordingly, even where the ultimate object was the sale of the Club, the avoidance of liquidation was a significant economic reason, justifying dismissal of the employees.

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