TRAVERS SMITH

Finance Monthly

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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 the *Cukorova* line of cases. 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 Developments

LIBOR has continued to command attention over the Summer. The Hogg Committee, tasked with selecting the new administrator for LIBOR has appointed NYSE Euronext Rate Administration Limited, a newly formed subsidiary of NYSE Euronext, which is expected to assume responsibilities in early 2014. The Screen Rate LMA language circulated in the Spring happily accommodates a successor change to BBA and the strong possibility of Reuters being replaced as the screen provider. New LMA language also addressed the removal of certain tenors by the BBA for certain currencies at the end of July by the introduction of "interpolation" language, and with effect from 1 July, bank rate submissions have been subject to a three month embargo by the interim administrator to remove the incentive to manipulate.

The US Federal Reserve and Treasury have supported statements from Gary Gensler, Chairman of the US Commodities and Futures Trading Commission who has stated that LIBOR cannot be replaced and needs wholesale reform. NYSE Euronext, in its pitch to the Hogg Committee suggested that rates may be referenced to actual transactions reported to a trade repository and it remains to be seen whether the system adopted by the new administrator will fully address US concerns.

Over the last twelve months RBS, Barclays and UBS have each been fined heavily by UK and US Regulators, three individuals have so far been charged with conspiracy to defraud and in the Spring a new criminal offence of making misleading statements and creating misleading impressions in connection with the setting of financial benchmarks was introduced by section 91 of the Financial Services Act 2012. The European Commission is currently undertaking an anti-trust investigation into banks setting the LIBOR benchmark and its findings are expected by the end of the year. In addition, press reports have recently suggested that several significant pension funds are actively considering the pursuit of legal claims against banks fined for manipulation. Close attention will also be paid within the legal community to the outcome of Barclays' appeal (scheduled for Autumn 2013) against the decision in *Graiseley Properties v Barclays [2013]* permitting an amendment to an interest rate swap claim to accommodate allegations of fraudulent misrepresentation arising from the LIBOR manipulation. Barclays' appeal follows the unsuccessful attempt to similarly amend a claim against Deutsche Bank in *Deutsche Bank & Ors v Unitech Global & Ors [2013]*.

Basel III and Increased Costs

The LMA has amended its footnotes to the Increased Costs clauses in its suite of documents to draw attention to the fact that the European legislation setting out the new standards for bank capital and liquidity requirements has now been published. Accordingly there are doubts as to whether the Basel III proposals can be characterised as a "change in law" in documents now being signed. Lenders need to give careful consideration to whether Basel III is to be outside or within the scope of the Increased Costs clause. A subsequent footnote to the LMA clause which excludes increased costs arising from Basel II as giving rise to an increased costs indemnity payment, but which carefully carves out Basel III from that exclusion, may no longer be sufficiently specific.

"Big Four Only" Clauses

On 24 July 2013, the Competition Commission published its provisional conclusions on auditor appointment. These require, inter alia, mandatory retendering every five-seven years (although not compulsory rotation of auditors). The report also focuses on provisions within facility agreements which limit the selection of auditors to the four major accounting firms. It proposes to recommend to the LMA that the definition of "Auditors" within its Leveraged Facility Agreement be amended so that it does not limit a company's choice of auditors to a pre-selected list. The LMA definition is square bracketed, not mandatory and

Spotlight on…the Cukorova Saga

The *Cukorova* line of cases, originating in the courts of the British Virgin Islands in 2007 and culminating in three visits to the Privy Council has afforded a valuable judicial analysis of the Financial Collateral Arrangements (No. 2) Regulations 2003 (the "FC Regulations") and a demonstration of the pragmatic application of equitable principles in the common law system. Privy Council decisions are not binding on the courts of England and Wales, but since the court is populated by Supreme Court judges, they are highly persuasive.

In pursuit of its aim to achieve ownership of Cukorova's shareholding stake in Turkcell, the main Turkish mobile phone network provider, ATT lent money to Cukorova and took a share mortgage over Turkcell shares which specifically incorporated, not unusually, the power to appropriate under the FC Regulations. This enabled ATT to enforce the share mortgage by appropriating the mortgaged shares in satisfaction of the liabilities owed to ATT. The power of appropriation on which, prior to *Cukorova*, there was little case law is a potentially powerful remedy which permitted ATT as mortgagee to take ownership of the shares (essentially eliminating the equity of redemption) in circumstances where prior to the FC Regulations, a foreclosure order would have had to be obtained from the court. Under English law, a foreclosure order affords a 6 month opportunity for the debt to be repaid by the mortgagor and the mortgaged property redeemed.

A succession of cases progressed through the BVI courts during which the right of ATT to accelerate the loan and appropriate the shares was vigorously contested. In January 2013, the Privy Council upheld the validity of ATT's actions, notwithstanding that Cukorova had, within a month of acceleration, tendered the full amount of debt to ATT and maintained that sum in a segregated account for three years. ATT's objectives, however, were frustrated by the Privy Council's determination (by application of equitable principles more frequently encountered in cases of lease forfeiture) that relief from forfeiture was available against payment of a redemption sum by Cukorova. On 9 July 2013 the Privy Council concluded that Cukorova should pay a redemption sum (within sixty days – recently extended indefinitely to accommodate blocking proceedings instituted by ATT before the US courts) on terms which essentially deprived ATT of its contractual default interest return on $1.35bn for six years. The court was divided on the rationale for this. The majority of the Board concluded that ATT's appropriation of shares discharged the loan debt. The minority insisted that the contractual debt obligation remained, but default interest ceased to accrue on Cukorova's tender of principal. The English courts will eventually need to resolve this important issue.

already allows alternative auditor appointment subject to the reasonably exercised discretion of the Majority Lenders. The exact nature of the recommendation will be of interest, as will the LMA response.

Game for Court of Appeal

The case of *Leisure Norwich (II) Limited v Luminar Lava Ignite Limited and others [2012]* established the principle that where rent falls immediately before a company goes into administration, that rent does not constitute an administration expense. Conversely, the case of *Goldacre (Offices) Limited v Nortel Networks UK Limited [2009]* provided that rent payable in advance and falling due during the administration would constitute a prioritised administration expense. The somewhat arbitrary result of these cases has been judicially criticised (Morgan J.) and has resulted in the transparent appointment of administrators soon after the traditional rent quarter date, thus achieving almost a quarter of rent-free occupation to the obvious benefit of creditors to the company and the disadvantage of landlords. In *Re Games Station Ltd and others [2013]* the High Court followed *Luminar*, thus maintaining the status quo, but gave permission for a fast tracked appeal to the Court of Appeal. The Court of Appeal decision, which is expected in early 2014, is awaited with interest.

Barclays v Unicredit appealed

Unicredit has recently been granted permission to appeal the case of *Barclays Bank PLC v Unicredit Bank AG and another [2012]*. The Commercial Court determined that Barclays were entitled, as a condition of its consent to early termination of a guarantee commitment, to insist that its quarterly fee return over a five year period should be paid in full notwithstanding the contractual requirement to exercise its consent in a "commercially reasonable manner".

FATCA postponement

On 12 July 2013, the IRS announced various extensions, including an additional six months (to 1 July 2014) prior to the commencement of withholding on US source income payments to non-compliant FFIs and a similar grace period for the grandfathering regime, which now accommodates obligations advanced or committed prior to 1 July 2014.

In the courts

Harvey v Dunbar Assets plc [2013] EWCA Civ 952

The Court of Appeal (CA) considered whether, on the construction of a composite joint and several guarantee, one of four intended guarantors who signed the guarantee was liable, where one of the other intended guarantors had not signed the document. One of the signatures was held to have been forged. The effect of this was not to impair the validity of the guarantee given by that intended guarantor, but rather that no liability under the guarantee had arisen in the first place. Applying the modern approach to construction, the CA held that there was no express or implied provision displacing the prima facie position that all four intended guarantors had to sign for liability under the guarantee to arise. Therefore, the signatures of all four intended guarantors were an essential precondition to the liability of each guarantor. Each guarantee, however, would need to be considered on its own merits. Text within the guarantee which implied that the guarantee was not intended to be a single, composite document might incline the court to a different conclusion.

Redstone Mortgages Limited v Wiemer [2013] WL 2460319

Where a mortgage contract's provisions relating to the service of documents have been complied with, service will be deemed to have taken place. The claimant lender had sent a notice by way of letter of demand to the borrower, who had defaulted on his loan. The borrower denied he had received the letter and claimed the lender failed to serve the demand correctly. The contract specified (in conformity with the formulation in many similar documents, including the LMA suite of documents) that a notice would be treated as having been given on the second working day after the date of posting, even if it never arrived or was returned undelivered. The court held that there was no evidence to dispute that the lender had sent the notice, so (unless the borrower properly notified the lender of a new address, which he did not) the letter of demand was valid.

In the matter of the Nortel and Lehman Companies [2013] UKSC 52

As widely reported, the Supreme Court handed down its judgment in the Nortel/Lehman Brothers appeals. The Supreme Court held that a financial support direction or a contribution notice issued by the Pensions Regulator against a company after it goes into administration or liquidation is a provable debt (but does not have priority ranking as an expense of the administration or liquidation). The Supreme Court dismissed the arguments put forward by the Lehman administrators that such liabilities should be treated as 'non provable liabilities' (the so-called 'black hole' result).

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