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 Interest Rate Swap Mis-selling. Please get in touch if it raises any issues that you would like to discuss.
Jeremy Walsh, Head of Banking and Corporate Recovery Department

New Company and LLP Charges registration regime

On 9 August, BIS published draft regulations and explanatory notes revising the CA 2006 Part 25 regime regulating the registration of security created by companies and limited liability partnerships. Further comment is invited prior to 7 September 2012, but the regulations are expected to be laid before parliament in the Autumn and to come into force on 6 April 2013. One of the most radical changes to current practice will be the opportunity to file electronically, a process to be delineated by further regulations. The revised regime imposes a 21 day deadline for filing, as is currently the case, but significant changes include:

- the removal of criminal sanctions for failing to register a registrable charge (but the retention of the principle that security which is not properly registered will be invalid against liquidators, administrators and creditors of the chargor);
- the assumption that all charges (other than limited exceptions set out in the regulations) can be registered;
- the simplification of the registration process by the provision of a brief statement of particulars and the filing of a copy of the entire security instrument (which will be available for public inspection with limited redaction possibilities); and
- the abolition of the requirement (so far as UK companies and LLPs are concerned) to maintain registers of security.

Certain noteworthy developments are that (a) the latest regulations omit a previously explicit statement that security interests arising by operation of law are excluded from the registration process; and (b) a new provision in the regulations suggests that only third parties taking a charge will have constructive notice of charges disclosed on the register at the time the new charge is taken.

LIBOR – Wheatley Review

On 10 August, a discussion paper was issued by HM Treasury outlining provisional thoughts on the London Interbank Offered Rate (LIBOR) review being undertaken by Martin Wheatley, the designated head of the Financial Conduct Authority. Comments on the paper are invited by 7 September, with a view to the presentation of findings to the Chancellor of the Exchequer within the same month and the inclusion of legislative changes into The Financial Services Bill 2012-13. The discussion paper anticipates increased institutional oversight of the LIBOR process to increase transparency and objectivity (the British Bankers' Association currently supervises LIBOR setting); improving the LIBOR calculation mechanism; and enfolding the process within the regulatory framework established by the Financial Services and Markets Act 2000.

FATCA: All wrapped up?

FATCA, which subjects financial institutions to US withholding taxes absent comprehensive disclosure to the IRS with respect to US tax payers, has presented a number of difficult issues to the financial community, compounded by the impenetrable complexity of FATCA and its associated regulations. For practitioners, the issues include such fundamental matters as the proper allocation of risk between lender and borrower; the precise applicability of grandfathering arrangements; the nature and volume of the information required to be disclosed by compliant Foreign Financial Institutions (FFIs); and whether such disclosure would breach local bank confidentiality laws. Even the basic applicability of the FATCA regime to a loan relationship is beset with confusion. One might have concluded that if a borrower and its group had no US nexus and if payments were not sourced from the US FATCA withholding could be ignored. The "pass-thru" withholding concept, however may still apply in these circumstances.

Spotlight on… Interest Rate Swap Mis-selling

The scheme of redress and review agreed between the FSA, Barclays, HSBC, Lloyds, RBS and seven additional banks this summer following the FSA's review of the sale of interest rate hedging products, afforded some relief to those customers (somewhat arbitrarily classified as non-sophisticated) who satisfied two out of three conditions based on turnover, balance sheet size and employee numbers. Sophisticated customers and non-sophisticated customers who were not sold structured collar products and/or are unsatisfied with the proposed redress are obliged to pursue their claims through the courts. Proactive claims managers have predicted aggregate claims exceeding those resulting from PPI mis-selling. Is this a realistic expectation? A simple argument to the effect that a customer was inappropriately persuaded to accept an arrangement fixing his interest rate obligations against a background of falling interest rates is perhaps as obtuse as an objection to the payment of insurance premiums over a period during which no claims have arisen. Both products are perfectly rational responses to the amelioration of risk. More credible claims, based on unexplained and significant break costs, particularly if they arise in conjunction with long term hedging products mismatched to a loan term or pursuant to swap termination rights exercisable unilaterally by the provider or a requirement to effect a hedge with a lender as a condition of its loan can of course be envisaged.

Blithe assumptions that a failure to comply with the FSA Conduct of Business Sourcebook (CoBS) requiring *inter alia* the provision of information in comprehensible terms may however be misplaced. A recent Scottish Court of Session decision anticipated as potentially "opening the floodgates" has found in favour of RBS. The judgment which is of only marginal persuasiveness so far as the English courts are concerned, placed great emphasis on the RBS Terms of Business, a copy of which had been previously signed by the customer and which included non-reliance terms requiring the customer to take independent advice. The Judge, whilst acknowledging that the customer was a small property company inexperienced in complex financial instruments, also rejected the application of UCTA 1977 and any common law duty of care arising independently of the contractual terms. The Judge found further that a breach of the CoBS did not give rise to civil actions for breaches in circumstances where the customer was a corporate suffering loss in the course of carrying on a business. For now, the floodgates remain closed.

Where the loan is syndicated, a principal or interest payment made by a compliant FFI facility agent to a non-compliant FFI lender will under the current pass-thru payment regime, be subject to a withholding based on a rather arbitrary analysis of US assets owned by the compliant FFI party. In these circumstances, potentially contentious issues arise as to the allocation of risk between borrower and lenders.

Some of these issues have been resolved by the recent publication of the basic inter-governmental agreement between the US and UK, France, Germany, Italy and Spain. This will obviate direct disclosure to the IRS and permit presentation of information to the domestic revenue authorities, with any local disclosure/confidentiality issues no doubt resolved. Payment from borrowers with a US nexus or derived from a US source within the relevant jurisdiction will not be subject to withholding. In addition, a payment by a compliant FFI in one of the five jurisdictions to other non-compliant FFIs in the context of a syndicated loan relationship will not be subject to a withholding pursuant to the pass-thru regime if the payments are not US sourced. If the payments are US sourced, however, a pass-thru withholding may still apply and the same issue of risk allocation will arise. Other issues remain. Domestic recording systems need to be established by the end of 2013; it is not yet clear how many other jurisdictions are signed up to inter-governmental agreements; and contracting parties may still need to protect their position by policing transfers to non-compliant FFIs and anticipating circumstances in which counterparties fail to comply with reporting obligations.

In the courts

Cartwright & Another v The Registrar of Companies [2012] EWCA Civ 1159

This is an appeal to the CA following the pragmatic decision of Briggs J in *Re Globespan Airways Limited [2012] EWHC 359(Ch)*. Globespan went into administration by court order in December 2009 on terms that the administrators term of office would expire after one year, on 17 December 2010. The administrators decided to convert the administration into a creditors' voluntary liquidation (CVL), and sent the Registrar of Companies a notice in accordance with paragraph 83 of Schedule B1 of the Insolvency Act 1986. The administrators signed a conversion notice on 13 December 2010, which was receipted by the Registrar on 14 December 2010 but subsequently rejected because a box requiring the address of the liquidators (who were the same as the administrators) had not been completed. Correcting notices were served after the administrators ceased to hold office on 17 December 2010. Briggs J held that the correct date for commencement of the CVL was the date of receipt of the notice on 14 December 2010, rather than the eventual date of registration of the notice on 4 February 2011. If the CVL had commenced on 4 February 2011, there would have been an unfortunate "gap" between 17 December 2010 and 4 February 2011, during which control of Globespan would have devolved to the directors and there would have been an impact on the "relevant time" from which preference or transactions at an undervalue claims could be brought. Arden LJ, giving the CA judgment, noted that in the Globespan case, preferential claims of creditors would have been much smaller if the date of commencement of the CVL had been 4 February 2011. Nevertheless, the CA, overturning Briggs J decision, held that (a) the conversion date (from administration to liquidation) was 4 February 2011, when registration (not receipt) of the notice took place; but (b) the administrators had competency to effect the conversion after 17 December 2010, because "by implication" the administrators' term of office may be "automatically extended" in appropriate circumstances.

National Merchant Buying Society v Bellamy and another [2012] All ER 325

The Society had advanced a loan to CTF and following default, sought to recover under a guarantee provided by Bellamy and another. The guarantors denied liability, arguing absence of consideration, economic duress and/or undue influence. The court determined that forbearance by the Society from expelling CTF as a member of the Society (for failure to timely provide accounts) constituted good consideration, regardless of whether or not CTF was aware of the expulsion right; that the Society's threat to withdraw credit unless the guarantee was provided lacked the quality of illegitimacy necessary to constitute economic duress; and that Bellamy, who alleged that he had not been adequately advised before giving the guarantee, had not demonstrated that a relationship of dependence existed which might warrant a claim of undue influence. He was an experienced businessman who could have obtained legal advice independently.

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