Recent Fifth Circuit Decision Highlights Importance of Clarity and Specificity When Discussing Terms of Loan Trade

A recent Fifth Circuit decision serves as a reminder to loan market participants that they should choose their words very carefully when discussing terms of a trade over the telephone. The Fifth Circuit Court of Appeals recently ruled that a bank loan purchaser can pursue a breach of contract claim against a seller that, the purchaser claims, wrongfully backed out of a deal. In *Highland Capital Management, L.P. v. Bank of America, National Association,*[1] the Court reversed a decision by the District Court for the Northern District of Texas dismissing a breach of contract claim brought by Highland Capital against Bank of America over a debt trade. The Fifth Circuit found there was sufficient ambiguity regarding the parties' dealings to warrant a deeper look into the trade in order to discern whether the parties intended to be bound by the deal they reached over the phone.

According to Highland Capital (the "Purchaser"), in late 2009 it made a deal with Bank of America (the "Seller") to buy an interest in certain bank debt (the "Regency Loan"). In December 2009, the Purchaser's representative called the Seller's representative to finalize the terms. According to the Purchaser, the parties agreed in the phone conversation to all material terms of the trade, including the description, amount, and price. Based on industry practice and the parties' prior dealings, the agreement also incorporated the Standard Terms and Conditions for Distressed Trade Confirmations (the "Standard Terms") published by the Loan Syndications and Trading Association, Inc. (the "LSTA"),[2] which provides that an oral debt trade agreement is binding on the parties, so long as such agreement includes all material terms of the trade.[3] The Purchaser maintains that the

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[1] *Highland Capital Mgmt., L.P. v. Bank of Am*., 698 F.3d 202 (5th Cir. 2012).
[2] The Loan Syndications and Trading Association publishes Standard Terms and Conditions for Distressed Trade Confirmations, which governs certain terms and conditions for the trading of distressed debt in the secondary market. The parties may also agree to incorporate additional specific terms in a given transaction.
[3] *Id*. at 204.

Seller did not reserve any non-LSTA Standard Terms or other non-industry standard terms or conditions during the phone call.

Shortly after the initial conversation, the Purchaser memorialized the terms of the trade in a confirmatory e-mail. The Seller responded with an e-mail that stated the trade was "subject to appropriate consents and documentation."[4] The Purchaser believed that this "subject to" language only called for the incorporation of LSTA Standard Terms in the agreement. It did not undermine the enforceability of the original deal reached over the phone, nor did it permit either party to demand that non-industry or non-LSTA Standard Terms be included in the agreement.

The Seller refused to settle the trade unless the Purchaser agreed to the additional terms. In response, the Purchaser filed suit against the Seller for, among other things, breach of contract claiming that the terms sought by the Seller departed from the parties' oral agreement. Because the Regency Loan paid off at 100% of par, the Purchaser also claimed that the Seller's failure to settle the deal caused the Purchaser to lose the increased value of the principal of the Regency Loan.

The Purchaser took the position that the parties entered a binding and enforceable oral agreement on the phone which, pursuant to the agreed-to LSTA Standard Terms and the parties' past dealings, did not permit the addition of non-industry terms or conditions. The Purchaser claimed that the "consents and documentation" referenced in the Seller's confirmation e-mail were themselves constrained by the LSTA Standard Terms, such that any terms deviating from the LSTA Standard Terms were required to be expressly reserved when the parties made the agreement by phone. According to the Purchaser, the LSTA Standard Terms specify that "a party must expressly reserve any non-industry standard terms at the time the agreement is reached by phone call, e-mail or otherwise, or else those terms are waived and the agreement is a binding and enforceable contract."[5]

The Seller subsequently filed a motion to dismiss the case and the District Court granted the motion. Relying on the "subject to" language, the District Court held that the Purchaser failed to state a claim for breach of contract because the "subject to" language in the confirmation e-mail indicated that the parties did not intend to be bound without additional "consents and documentation" and that, consequently, no binding contract was formed during the phone call or in subsequent e-mails.[6]

The Fifth Circuit reversed the District Court's dismissal of the breach of contract claim, holding that when viewed in the light most favorable to the Purchaser, and taking all allegations as true, the Purchaser's complaint made a viable claim for breach of an oral contract. The Purchaser alleged in its complaint that, notwithstanding the subsequent e-mails, the parties entered a binding and enforceable agreement by phone. This agreement was one that, based on the allegedly agreed-to LSTA Standard Terms, was not subject to any additional, non-industry standard terms or conditions. The Fifth Circuit remanded the case to the District Court for further proceedings at which evidence adduced will be used to discern the true intent of the parties. The case is scheduled for trial beginning in September 2013. In the meantime, on February 22, 2013, the Seller moved for summary judgment alleging, among other things, that as a matter of law, no contract was formed by the parties. The Buyer filed its opposition to the Seller's summary judgment motion on April 12, 2013.

This decision underscores the potential ambiguity inherent in communications by phone and by e-mail which can bring risk and uncertainty into a deal. While a written confirmation is a standard industry practice, a contract may be

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4 *Id*.
5 698 F.3d at 207.
6 *Id*.

formed before anything is put in writing. LSTA trades are governed by New York law which specifically exempts loan trades from the statute of frauds.[7] Accordingly, parties may enforce oral contracts, as long as the parties intend to be bound at the time the agreement is made.[8] The issue in this case was the intent of the parties as to the material terms of the trade and their intent to be bound, which the Courts had a great deal of difficulty discerning.

Because oral agreements can be binding and enforceable, traders should clearly and explicitly state all material terms of the deal and be very specific about any intention to incorporate any non-market standard terms and conditions into the deal. Using best practices such as these will alleviate risk and provide useful tools should a dispute regarding the trade arise.

We will continue to monitor the case for further developments.

[7] See New York General Obligations Law § 5-701(b).
[8] 698 F.3d at 207.

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