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Briefing note

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Bank defeats swaps misselling and LIBOR claims

In the first case involving allegations about the rigging of LIBOR to reach judgment on the facts in England, the High Court has rejected wide-ranging claims that a bank missold interest rate hedging products. The Court concluded that the contractual terms and nature of the relationship blocked the claims based on the effect of the swaps and, while there was an implied obligation regarding the setting of LIBOR, it was narrow in scope, had not been relied on, and had not been broken.

The trial in *Property Alliance Group Ltd v The Royal Bank of Scotland plc* [2016] EWHC 3342 (Ch) lasted 38 days, and Asplin J's judgment runs to 187 pages. Despite the length, the judge ultimately gave short shrift to the claims. The claimant (C) failed to make out its claims either in fact or in law. The interest rate hedging products, entered into between October 2004 and April 2008, had resulted in C's missing out on the full benefit of the low interest rates that have followed the global financial crisis but, as a sophisticated commercial counterparty with professional advice dealing at arms' length with the bank, C could not visit the commercial consequences on the bank.

C was a property company with extensive loans from the bank. C's claims concerned swaps of varying degrees of complexity entered into to hedge C's interest rate exposure. The claims fell into three broad categories: first, misselling, involving misrepresentations and implied contractual terms; secondly, the internal management of the bank's relationship with C; and, thirdly, misrepresentations and implied terms with regard to the setting of LIBOR, on which swaps were based.

Misselling claims are always heavily dependent on their individual facts, but the LIBOR claims in *Property Alliance Group* have attracted particular interest. Claims of this sort are a recent innovation in the light of the regulatory investigations into LIBOR that have led to significant fines being imposed on banks, to criminal convictions for traders and to the reform of the way in which LIBOR is managed and set. Nevertheless, the LIBOR claims failed along with the more traditional misselling claims.

Key issues

- Importance of no reliance provisions in contracts emphasised
- Entering into a contract based on LIBOR does not entail a representation about the setting of LIBOR
- Implied contractual term about LIBOR limited to the currency and tenor in question

Misselling

The parties agreed that the bank did not owe any general duty to advise C in relation to the swaps the parties entered into. Instead, C alleged that, having offered an explanation about the swaps, the bank was under an obligation to ensure that its explanation was full, accurate and proper. In particular, C complained that the bank had failed to provide indications, including worked examples, of the break costs for terminating the swaps.

The judge concluded that the bank owed no such duty to C on the facts. The bank had to take reasonable care as to the accuracy of what it actually said, but that did not bring with it any wider duty. A duty to advise was expressly excluded by the relevant documentation and the commercial nature of the parties' relationship. There was no duty to provide details of break costs, and doing so was not market practice at the time.

C went on to allege that the bank had represented that the products were suitable as "hedges" for C's interest rate risk. C alleged that the transactions were not hedges at all because, for example, they were not precisely aligned to C's borrowing and the bank had various options to terminate the transactions.

The judge did not accept that describing the products generically as "hedges" brought with it any representation upon which C could rely as to the quality of the transactions. In any event, the contractual terms provided that C had not relied on anything said by the bank; the claim was therefore contractually barred. Further, C had not relied on this supposed representation in entering into the transactions.

C also alleged that terms should be implied into the swap contracts and loan facilities that the swaps would be suitable for hedging C's interest rate risk, that the bank would act in good faith and in accordance with commercial fair dealing and that the bank would not withhold information. The judge saw no need to imply these terms, which she regarded as contrary to the express terms of facility agreements that excluded equitable and fiduciary duties. These terms were also unnecessary as between two sophisticated commercial parties negotiating at arms' length.

The bank's internal arrangements

C complained that the transfer of responsibility for the bank's relationship with C to the bank's Global Restructuring Group constituted a breach of the bank's obligations. The judge considered that C had no implied right to be managed by any particular team within the bank. That was an internal matter for the bank alone. In any event, there was no basis for the allegation that the internal transfer was irrational or done in bad faith.

C also contended that its agreements with the bank included implied terms that the bank would, in general, perform the agreements in good faith and not in a commercially unacceptable or unconscionable way. C also argued that where the bank had a discretion, it was obliged to exercise that discretion in good faith and not capriciously. C complained in particular about the bank's calling for valuations of C's property portfolio twice, its threatening to appoint receivers and its demanding a security review at C's expense.

Having rejected C's case regarding a specific implied term of good faith regarding hedging, Asplin J also rejected C's contention of an even wider obligation of good faith. She observed that there is no general duty of good faith in English law, and concluded that a term of this sort should not be implied into standard banking documentation.

The judge accepted that where a party has a discretion to make an assessment or choose from a range of options, there will normally be an implied a term of the sort alleged by C. But she did not consider that the bank's rights in this case fell within that category. The bank had an absolute right to call for a valuation or a security review if it wanted to do so, not a discretion that required it to consider both parties' interests.

LIBOR

C alleged that the bank made wide-ranging implied representations regarding LIBOR, including that, on all dates up to entry of the swaps, LIBOR represented the interest rate as defined by the BBA (then responsible for LIBOR), that the bank had no reason to believe that LIBOR represented anything else and that the bank had not made false or misleading submissions regarding LIBOR. Alternatively, C argued that similar terms should be implied into the swap contracts.

The judge accepted there is a common assumption that parties will behave honestly, but she did not accept that representations of the sort asserted by C could be implied merely from the bank's offering to enter into swaps based on LIBOR. Implied representations had to be based in conduct, and there was no relevant conduct on the bank's part from which the alleged representations could be drawn. Even if the bank had made any representations, the judge considered that they would have been limited to the bank's knowledge regarding the particular tenor and currency in question, not LIBOR generally. In any event, C failed to prove that it had relied on any representation regarding 3 month GBP LIBOR or that there was any relevant impropriety on the bank's part.

The judge did, however, conclude that a term should be implied into the swap contracts that LIBOR would be calculated in the way defined by the BBA, ie that the bank would make proper submissions regarding LIBOR. This implied term was limited to the tenor and currency to which the transaction related (3 month GBP LIBOR), not to LIBOR as a whole, and was only as to the bank's conduct, not the conduct of other LIBOR-setting banks. As a result, the bank's admission that its dealers had been involved in improper conduct regarding CHF and JPY LIBOR was irrelevant. C was unable to prove that the bank had acted in breach of its obligations regarding 3 month GBP LIBOR, and its claim therefore failed.

The other implied terms contended for by C were, the judge thought, both unnecessary and too vague.

Conclusion

C's claim involved throwing virtually every possible allegation at the bank. They all failed. When commercial parties are dealing with each other at arms' length and on terms that say that one is not relying on the other, the English courts will not in the main imply additional obligations. Commercial parties are expected to look after their own interests.

The general misselling claims pursued by C were typical of claims that have been brought against banks in the past (though very broad in scope), and the judge reached a conclusion similar to many of the other misselling claims that have reached a final decision.

The LIBOR-based claims are, however, a more recent creation. A key aspect of the judgment regarding LIBOR may prove to be Asplin J's decision that a bank makes no representation as to the setting of LIBOR merely by offering to enter into a contract based on LIBOR. If there had been a representation that was proved to be false (though C would in any event have failed on the facts in this case), the remedy would have been rescission, ie putting the parties in the position they would have been had the swap not been entered into, which would require the reversal of all payments made. The judge's acceptance that there is an implied term in a swap contract regarding LIBOR-setting may, at this distance from the global financial crisis and if that term is broken, give rise to a claim in damages, but damages are unlikely to be substantial.

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