

THE BANKING
LITIGATION
LAW REVIEW

SECOND EDITION

Editor
Christa Band

THE LAWREVIEWS

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PREFACE

As we noted in the Preface to last year's edition of the *Banking Litigation Law Review*, banks will always be regular litigants – generally as defendants – and this year's contribution of jurisdiction-specific chapters explains how and why.

The themes that emerge from the chapters that follow show that, almost uniformly, the number of cases that might be said to have their origin in the 2008 global financial crisis is reducing. That is partly because of the passage of time – even long-running litigation has to end at some point. It is also because the financial services industry and legal profession have benefited from the guidance given in decided cases. The principles so set reduce uncertainty in providing precedent and less formal indications of how claims will be received. Settlement is promoted – generally for the benefit of all parties and the courts.

There are also some interesting comments on what is being done in particular jurisdictions to provide for alternative means of resolving disputes – to keep them away from the civil courts altogether – or to encourage settlement with the usual savings of costs and court resources. Various countries are thinking about ways in which litigation can be made easier and more efficient – an aim not limited to banking litigation. One topic that is noted in several contributions is the approach of the courts and legislature to class actions. These cover a spectrum from well-established and often-used procedures (eg, the United States) to jurisdictions that have considered class actions and decided against their use (eg, Austria).

Also of interest on a comparative basis is the extent to which different jurisdictions balance contractual freedom and certainty against consumer protection. This is done in various ways through statutory control of contractual clauses (for example, as to interest rates or obligations that are considered unfair) and, importantly, exclusion clauses. Again, the regulatory overlay here is important. Some of the complaints that might otherwise have found their way to the courts are resolved – often more quickly, more cheaply and more effectively – through regulatory enforcement processes. They are strictly outside the scope of this edition, though the regulatory impact on the volume and kind of banking litigation with which the courts are faced cannot be ignored.

A further spectrum of approaches is clear in relation to the difficult issues of confidentiality and privilege. The application of the principles is often fact-sensitive. It has – perhaps as a result – generated significant litigation in more than one jurisdiction. Parties are likely, in the future, to have to weigh up the substantive benefit they hope to secure from the maintenance of privilege and to focus more strategically on how to protect privileged information where it matters most and yield to pragmatism in other respects. This is particularly acute at the interface between litigation and regulation.

If litigation is born in part of uncertainty, a common reflection in what follows is that economic and political change are likely to fuel claims in the future. The reasons for this are

various and complex. But any situation in which there is unpredictability means there are likely to be disappointed investors – the quintessential claimant in banking litigation claims. That is the recognised backdrop to much recent litigation. The changing political climate also dictates the regulatory agenda. For many jurisdictions, financial services regulation – which has a major impact on banking litigation – has become bigger and more complex year on year. In the United States, that position is now slowing or even reversing in some respects under the Trump administration, though how this will translate into banking litigation is not yet clear. Last year's edition noted that there will be changes to UK law as a result of its decision to leave the EU – and doubtless knock-on effects on litigation in the remaining EU states. It commented – in a way that now looks to have been over-optimistic – that this year's edition could address the issues. However, the clarity that the industry and profession seeks in this regard has not yet been achieved. By next year, it is hoped that substantive comment on what this is likely to mean for banking litigation will be possible.

Christa Band

Linklaters LLP

London

July 2018

AUSTRALIA

Ross Drinnan, Alexandra Mason and Laura Hablous¹

I SIGNIFICANT RECENT CASES

A number of significant banking litigation cases have been heard by Australian superior courts over the past year, although judgments in some of these have not yet been handed down. A number of important banking law cases are also currently before Australian courts. Current significant cases are focusing on issues such as benchmark manipulation, financial advice models and responsible lending practices.

Australian banks have experienced unprecedented parliamentary and regulatory interest in recent years, peaking with the commencement of a Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (discussed further in Section IX, below). Once this process has completed, there will almost certainly be follow-on litigation in relation to areas of misconduct identified in the course of the Royal Commission process.

i **Alleged failure to comply with anti-money laundering obligations – AUSTRAC v. CBA**

In August 2017, the Australian Transaction Reports and Analysis Centre (AUSTRAC), which is Australia's financial intelligence and regulatory agency, commenced proceedings against the Commonwealth Bank of Australia (CBA) for serious and systemic non-compliance with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF Act).² The claim alleges over 53,800 contraventions of the AML/CTF Act, including in connection with CBA's intelligent deposit machines (IDMs). AUSTRAC alleges, among other things, that CBA failed to properly assess the risks associated with IDMs before they were rolled out in 2012 and subsequently failed to give threshold transaction reports in respect of certain transactions either on time or at all. The maximum penalty for an individual contravention alleged in the amended statement of claim is up to A\$21 million.

On 4 June 2018, AUSTRAC and CBA announced that the parties had settled the proceedings on the basis that CBA would pay a penalty of A\$700 million. The parties will appear before the Federal Court seeking orders to give effect to the settlement sometime in the coming months. If approved by the Court, this will be the largest civil penalty in Australian corporate history.

¹ Ross Drinnan and Alexandra Mason are partners, and Laura Hablous is a senior associate, at Allens.

² NSD 1305/2017.

ii Personal advice and failure to act in customers' best interests – ASIC v. NSG Services Pty Ltd and other undecided matters

A significant volume of banking litigation in Australia is commenced by the Commonwealth financial conduct regulator, the Australian Securities and Investments Commission (ASIC), for breaches of the Corporations Act 2001 (Cth) and other legislation. The Corporations Act contains provisions, among other things, governing financial conduct. Where those provisions have been contravened, a court may grant relief including declarations, injunctions and, for some provisions, orders for compensation and civil penalties.

ASIC has now taken steps against several parties in respect of their compliance with the obligations amended into the Corporations Act in 2012 as part of the Future of Financial Advice (FOFA) reforms.³ The FOFA reforms introduced a duty for financial advisers to place the best interests of their clients ahead of their own when providing personal advice to retail clients.

In October 2017, the Federal Court imposed a civil penalty of A\$1 million against Melbourne-based financial advice firm NSG Services Pty Ltd (NSG) for breaches of the best interests duty introduced under the FOFA reforms.⁴ This represents the first finding of liability against a licensee for breach of the FOFA reforms, although the matter was resolved on a consensual basis so is of limited precedent value.

In December 2016, ASIC commenced proceedings in the Federal Court against two companies that operate as part of the Westpac group's wealth management business.⁵ The claim alleges that the companies provided 'personal advice' as defined in the Corporations Act, and, accordingly, failed to act in the customers' best interests as required by the Act. The concept of 'personal advice' has not previously been considered by the courts. The Court heard closing arguments on 16 February 2018 with judgment reserved.

iii Alleged manipulation of bank bill swap reference rate – ASIC v. Westpac Banking Corporation

In early 2016, ASIC commenced proceedings in the Federal Court against three of Australia's major banks, ANZ, Westpac and NAB, for alleged manipulation of the bank bill swap reference rate (BBSW).⁶ The BBSW is the primary interest rate at which banks lend to each other over short periods. It is an important interest rate in the Australian economy, providing a benchmark for the setting of various business loan rates.

ASIC claimed that each bank traded in a manner intended to create an artificial price for bank bills on multiple occasions. ASIC alleges that on these occasions each bank:

- a* had a large number of products that were priced or valued with reference to the BBSW;
- b* traded in the bank bill market with the intention of moving the BBSW higher or lower; and
- c* sought to maximise profit or minimise loss to the detriment of those holding opposite positions to their own.

3 See Corporations Amendment (Future of Financial Advice) Act 2012 (Cth).

4 *Australian Securities and Investments Commission, in the matter of NSG Services Pty Ltd v. NSG Services Pty Ltd* [2017] FCA 345 (30 March 2017 – judgment); *Australian Securities and Investments Commission, in the matter of Golden Financial Group Pty Ltd (formerly NSG Services Pty Ltd) v. Golden Financial Group Pty Ltd* (No. 2) [2017] FCA 1267 (proposed pecuniary penalties and costs orders).

5 NSD 2204/2016.

6 VID 197/2016, VID 282/2016; and VID 604/2016 respectively.

ANZ and NAB entered into enforceable undertakings with ASIC in relation to each bank's bank bill trading business and their participation in the setting of the BBSW. The Federal Court found that both ANZ and NAB had attempted to engage in unconscionable conduct, and imposed pecuniary penalties of A\$10 million each.⁷ The Court also noted that ANZ and NAB will give enforceable undertakings to ASIC to take certain steps and to pay A\$20 million applied to the community benefit and A\$20 million towards ASIC's investigation and other costs.

The Westpac proceedings proceeded to trial in October 2017. On 24 May 2018, Justice Beach handed down a 643-page judgment in the proceeding.⁸ In summary, Beach J:

- a rejected ASIC's case that Westpac contravened Sections 1041A and 1041B of the Corporations Act, finding that Westpac did not engage in market manipulation or market rigging on any of the specific contravention dates alleged by ASIC;
- b rejected ASIC's general allegation that Westpac had systematically traded with the sole or dominant purpose of influencing the level at which the BBSW was set in a way that was favourable to Westpac and that therefore resulted in yields that did not reflect the forces of genuine supply and demand;
- c found that Westpac had contravened the Australian Securities and Investments Commission Act 2001 (Cth) (the ASIC Act) by engaging in unconscionable conduct on four occasions in 2010, when Westpac traders traded with the dominant purpose of influencing the level at which BBSW was set on those dates. In making this finding, his Honour did not find that Westpac had in fact affected the level of BBSW on those dates; and
- d found that Westpac had contravened its supervisory duties as an Australian financial services licensee under Section 912A of the Corporations Act.

The matter will now go to a hearing on penalty. The maximum penalty for contraventions of the relevant sections of the ASIC Act is A\$1.1 million per contravention.

ASIC commenced similar proceedings in the Federal Court against CBA on 30 January 2018.⁹ CBA and ASIC have agreed an in-principle settlement, which is subject to approval by the Court.

iv Alleged breach of responsible lending obligations in relation to home loans – undecided

In March 2017, ASIC commenced proceedings in the Federal Court against Westpac for alleged breaches of laws relating to responsible lending.¹⁰ The National Consumer Credit Protection Act 2009 (Cth) (NCCPA) contains consumer protections to ensure that credit providers make reasonable inquiries about a borrower's financial situation and assess whether a particular loan will be unsuitable. ASIC alleges that between 2011 and 2015 Westpac failed to assess properly whether borrowers could meet their repayment obligations before allowing those customers to enter into home loan contracts.

7 *Australian Securities and Investments Commission v. National Australia Bank Limited* [2017] FCA 1338; see also ASIC Media Release dated 20 November 2017.

8 *Australian Securities and Investments Commission v. Westpac Banking Corporation (No. 2)* [2018] FCA 751.

9 *Australian Securities and Investments Commission v. Commonwealth Bank of Australia* (VID65/2018); see also ASIC Media Release dated 30 January 2018.

10 NSD 293/2017.

ASIC states that the bank:

- a used a benchmark instead of the actual expenses declared by borrowers in assessing their ability to repay the loan;
- b approved loans where a proper assessment of a borrower's ability to repay the loan would have shown a monthly deficit; and
- c for home loans with an interest-only period, failed to have regard to the higher repayments at the end of the interest-only period when assessing the ability to repay.

Westpac is defending the claim. The hearing will commence in September 2018.

ANZ has also been the subject of proceedings in relation to breaches of the responsible lending provisions under the NCCPA by its former car finance business, Esanda.¹¹ ASIC alleged that ANZ failed to meet its responsible lending obligations when relying only on payslips to verify the consumer's income, in circumstances where it knew that payslips could be easily falsified and it had reason to doubt the reliability of information from the particular broker businesses. ASIC and ANZ filed a statement of agreed facts and admissions and the Court ordered ANZ to pay a penalty of A\$5 million.

II RECENT LEGISLATIVE DEVELOPMENTS

The Treasury Laws Amendment (Banking Executive Accountability and Related Measures) Act 2018 (BEAR) came into force on 1 July 2018 for large authorised deposit-taking institutions. Under BEAR, senior executives must be registered with the Australian Prudential Regulation Authority (APRA) along with details of their specific responsibilities. The APRA has been provided with increased powers in order to strengthen its ability to hold banks and their executives accountable, including the ability to charge fines, disqualify individuals and impact remuneration policies. It remains to be seen what litigation may arise as a result of the introduction of these new requirements.

Amendments have also been made to the Corporations Act 2001 (Cth) in order to address the alleged conduct that was the subject of the proceedings in relation to manipulation of the benchmark rate.¹² The amendments establish a new licensing regime requiring administrators of designated significant financial benchmarks to obtain a 'benchmark administrator licence' from ASIC.¹³ Under this new regime, there are new offences and penalties for manipulation of financial benchmarks¹⁴ and ASIC has new powers to make rules imposing a regulatory framework for licensed benchmark administrators.¹⁵

III CHANGES TO COURT PROCEDURE

In October 2016, the Federal Court implemented a series of new practice notes, including the 'central practice note' and a practice note for the 'commercial and corporations' practice

11 *ASIC v. ANZ* [2018] FCA 155.

12 Corporations Act 2001 (Cth), Part 7B.

13 Corporations Act 2001 (Cth), Section 908BA.

14 Corporations Act 2001 (Cth), Sections 908DA and 908DB.

15 Corporations Act 2001 (Cth), Sections 908CA and 908CD.

area (C&C-1). As set out in C&C-1, the Court is currently experimenting with a new form of commencing proceedings, which it is thought will make it easier for parties, including ASIC, to commence proceedings.

The Federal Court now provides an option for an applicant to commence proceedings by way of a 'concise statement', not exceeding five pages in length, and summarising the important facts giving rise to the claim, the relief sought, the causes of action for the relief sought and the alleged harm suffered. The judge at the first case management hearing maintains a wide discretion in deciding how the case should proceed thereafter.

IV INTERIM MEASURES

Acts and court rules across the various Australian jurisdictions provide that a court may grant an interim injunction where there is an urgent need to maintain the *status quo*. They operate to prevent a person from acting in a way that would cause irreparable damage to the applicant before a judicial decision can be obtained. A party will ordinarily make an application for an interim injunction *ex parte* and, as such, will be under an obligation to disclose all relevant facts. The court will require that the applicant provide an undertaking as to damages to ensure that the respondent can be compensated for any loss flowing from the award of the injunction.

Australian courts also have jurisdiction to award *Mareva* orders¹⁶ (freezing orders), which restrain a defendant from dealing with assets in such a way that would defeat the effect of a judgment favourable to the plaintiff. Court rules across the jurisdictions create distinct and additional powers to grant freezing orders.

V LAWYER-CLIENT PRIVILEGE

Parties to litigation in Australia may be required to disclose documents in their possession or control that are relevant to the issues in dispute. At the investigation stage, most regulators also have the power to compel persons to produce documents.

Lawyer-client privilege, however, operates to allow persons to prevent the disclosure of certain documents. A client may claim privilege in relation to confidential communications between a client and lawyer made for the dominant purpose of the client seeking or being given legal advice (client legal privilege). Similarly, confidential communications between a client and another person, or the lawyer and another person, for the dominant purpose of the client receiving legal services in relation to actual or anticipated litigation are also protected (litigation privilege).

Privilege can be waived at any time by a party acting inconsistently with the maintaining of privilege, including by disclosing the substance or effect of the relevant communication.

In-house lawyers are accorded the same status as external lawyers for the purposes of privilege protections. That said, claims for privilege involving in-house lawyers can be the subject of additional scrutiny in circumstances where it is questionable whether the lawyer has the necessary degree of independence or also has a non-lawyer role within the company.

¹⁶ As recognised by the English Court of Appeal in *Mareva Compania Naviera SA v. International Bulkcarriers SA* [1980] 1 All ER 213.

VI JURISDICTION AND CONFLICTS OF LAW

Banks and other financial institutions in Australia are largely governed by federal legislation.¹⁷

Banking litigation may be commenced in either the federal or state courts, depending on whether it arises as a result of legislation, common law or in equity. Although the majority of relevant legislation is federal, there remains an active banking litigation practice in state courts dealing with a range of matters, including the enforcement of loans and questions of fiduciary duties. State courts are also able to exercise limited federal jurisdiction under the principle of accrued jurisdiction.

Few conflicts of law issues arise in banking disputes. In circumstances where a conflict exists between the applicable law of a state or territory and a federal law, pursuant to Section 109 of the Australian Constitution, the federal law prevails to the extent of any inconsistency. Where a conflict exists between two state or territory laws, the issue is usually determined by reference to similar choice of law considerations that apply to the determination of whether a foreign jurisdiction is the most appropriate forum.¹⁸

Many disputes between consumers and financial services providers are not determined in courts but by external dispute resolution (EDR) schemes with jurisdiction to determine disputes between consumers, including small businesses, and financial services providers.¹⁹ These include:

- a* the Financial Ombudsman Service, an ASIC-approved EDR scheme that considers disputes relating to banking and finance, insurance, financial planning, funds, mortgage and finance broking, estate planning, and management and trustee services;
- b* the Credit and Investments Ombudsman, a separate ASIC-approved EDR scheme; and
- c* the Superannuation Complaints Tribunal, a statutory body established under the Superannuation (Resolution of Complaints) Act in 1993 (Cth), which deals with decisions and conduct of trustees, insurers and other decision makers in relation to regulated superannuation funds.

VII SOURCES OF LITIGATION

Banking litigation is frequently initiated by individual customers, but over the past decade there has been a marked increase in customers challenging financial services firms by initiating class action proceedings. Adverse regulatory findings by regulators, such as ASIC, have also been a fertile source of banking litigation.

17 See, e.g., Banking Act 1959 (Cth); ASIC Act; Corporations Act 2001 (Cth); Competition and Consumer Act 2010 (Cth), Schedule 2 (Australian Consumer Law); National Consumer Credit Protection Act 2009 (Cth) and Schedule 1 (National Credit Code); Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth); Personal Property and Securities Act 2009 (Cth); Privacy Act 1988 (Cth), Schedule 1 (Australian Privacy Principles).

18 For example, in *John Pfeiffer Pty Ltd v Rogerson* [2000] HCA 36, the High Court held that the relevant choice of law consideration was where the tortious act occurred, rather than the forum that provided the greatest convenience to the parties.

19 If providing financial services to retail clients, financial services licensees are required by Section 912A(1)(g) of the Corporations Act to have adequate internal dispute resolution procedures and be members of an EDR scheme.

i Misleading or deceptive conduct, or unconscionable conduct

Allegations of misleading or deceptive conduct, or unconscionable conduct, are frequently raised in banking litigation.

The Corporations Act prohibits a person engaging in conduct, in relation to a financial product or a financial service, that is misleading or deceptive, or likely to mislead or deceive. The Act also prohibits a financial services licensee from engaging in conduct that is unconscionable. These prohibitions are also reflected in the Australian Consumer Law and ASIC Act. In addition to statutory claims, a claim in equity may be brought for unconscionable conduct.²⁰

If the court determines that misleading or deceptive, or unconscionable conduct (or a combination of these) has occurred, remedies may include compensation, financial penalties, variation or voiding of a contract, or a refund or performance of specified services.

By way of example of these claims, in *ASIC v. GE Capital Finance Australia Pty Ltd*,²¹ the Federal Court found that GE Capital had impliedly represented to credit card holders that they could not activate new credit cards, or apply for or obtain an increased credit limit, unless they agreed to receive invitations to do so. The Court held that this contravened provisions in the ASIC Act prohibiting misleading or deceptive conduct. A penalty of A\$1.5 million was imposed owing to the deliberate and systematic nature of GE Capital's conduct.²²

In addition, in *Violet Home Loans Pty Ltd v. Schmidt*,²³ the Victorian Court of Appeal held that the conduct of a mortgage originator and manager who had processed a loan application on behalf of a mortgagee was unconscionable under Section 12CB of the ASIC Act on the basis that the mortgagee was vulnerable and an 'unsophisticated and naïve man who had little financial nous',²⁴ and the mortgage originator was aware of irregularities in the loan application but had made no efforts to investigate them.²⁵ The Court held that while the conduct in question had to be more than negligent, 'recklessness, in the form of wilful blindness, may... supply the necessary element of moral obloquy'.²⁶ The Court affirmed the order to set aside the loan and mortgage.

ii Contractual disputes

A large number of banking disputes arise in the context of financial institutions enforcing their rights under loan agreements, and defending cross-claims by borrowers with respect to the validity or enforceability of such loan agreements. These contractual disputes often raise issues of greater significance to banking institutions.

Australia's unfair contract terms legislation,²⁷ which was extended in November 2016 to apply to standardised contracts with small businesses, is likely to continue to be a source of disputes between consumers, small businesses and financial institutions. Lenders have come under increasing pressure from regulators to review their standardised lending terms in light of the legislation, particularly in relation to entire agreement clauses, indemnification

20 See, e.g., *Commercial Bank of Australia Ltd v. Amadio* (1983) 151 CLR 447.

21 [2014] FCA 701 (*GE Capital*).

22 *GE Capital* [2014] FCA 701, [80], [93]–[94].

23 [2013] VSCA 56 (*Violet Homes*).

24 *Violet Homes* [2013] VSCA 56, [34].

25 *Violet Homes* [2013] VSCA 56, [68].

26 *Violet Homes* [2013] VSCA 56, [58].

27 Australian Consumer Law, Section 24; ASIC Act, Section 12BG.

clauses, terms relating to financial indicator covenants and unilateral variation clauses. In March 2018, ASIC released a report in respect of the changes to unfair contract terms in small business loans and noted that, as a next step, the banks were required to communicate these changes to small businesses via multiple channels and ASIC will continue to monitor the use of the changed terms going forward.²⁸

iii Regulatory investigations

Both ASIC and APRA have extensive powers to investigate financial institutions. These investigations may come about as a result of:

- a* monitoring and surveillance work;
- b* a member of the public, or a whistle-blower, reporting a financial institution's perceived misconduct;
- c* referrals from other regulators; or
- d* a financial institution's self-reporting.

iv Class actions

Australia has a well-developed class action regime and has seen a significant increase in the number of class actions over the past decade, particularly with the development of an active litigation funding industry and the promotion of claims by plaintiff law firms. Long-term trends of class actions in Australia suggest that financial institutions are the most frequent targets of class actions, with claims relating to the mis-selling of financial products, the rating of financial products, lending practices and compliance with trustee obligations most commonly in issue.

In October 2017, class action proceedings were filed against CBA, in connection with the AUSTRAC case discussed in Section I, above. The class action alleges that CBA engaged in misleading or deceptive conduct and that it failed to disclose material information to the market in relation to the aspects of its AML/CTF controls that are the subject of the AUSTRAC proceeding.

With the intense scrutiny on the financial services industry as a result of the Royal Commission (discussed in Section IX, below), there are already reports of pending class actions in relation to the areas of misconduct that have been the subject of the Royal Commission to date. For example, AMP is currently facing four class actions that allege, among other things, that it charged financial advice customers ongoing service fees where it was not providing any services; it made false or misleading statements to ASIC in respect of this practice; and that this conduct arose from inadequate monitoring, reporting and governance controls.

As the Royal Commission continues to explore instances of misconduct by financial institutions, there remains a very real risk of further class actions.

VIII EXCLUSION OF LIABILITY

Exclusion of liability is most relevant to disputes between financial services providers, rather than disputes with consumers, given the operation of the unfair contract terms legislation²⁹ described in Section VII.ii, above. In this context, exclusion clauses in consumer and small

28 See ASIC, 'Unfair contract terms and small business loans' (Report 565, March 2018).

29 Australian Consumer Law Part 2-3; ASIC Act Part 2, Division 2.

business contracts purporting to disclaim liability for representations made to prospective borrowers, including innocent and negligent misrepresentations included in a loan agreement, mortgage or guarantee are likely to be held unenforceable as a consequence of the unfair contracts legislation.

Unlike contracts between consumers and financial services providers, contracts between financial services providers themselves are generally not protected by consumer legislation. Financial services providers are viewed as often having equal bargaining power and not in need of the same kind of statutory protections afforded to consumers. At common law, operation of an exclusion clause is defined by the ordinary rules of contractual interpretation. Clear words are needed to rebut the presumption that contracting parties would not seek to abandon any remedies accruing from a breach of contract.³⁰

IX REGULATORY IMPACT

Increasing scrutiny by regulators and Parliament on financial institutions and their senior executives, as well as moves to provide regulators with broader powers (see Section II, above), feed into an active Australian litigation environment.

At present, the main focus for the banking and financial services industry is the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. The Royal Commission's terms of reference require the Commissioner, the Honourable Kenneth Hayne AC QC, to inquire into a broad range of matters, including:

- a* whether any conduct by financial services entities might have amounted to misconduct;
- b* whether any conduct, practices, behaviour or business activities by financial services entities fall below community standards and expectations;
- c* whether any misconduct is attributable to the particular culture and governance practices of a financial services entity or broader cultural or governance practices in the relevant industry or subsector; and
- d* whether any changes to the legal framework, practices within financial services entities and the financial regulators are necessary to minimise the likelihood of misconduct by financial services entities in the future.

The Commissioner's final report is expected no later than 1 February 2019. The conclusions reached by the Commission will have significant implications for all of the areas considered in this publication going forward, including the regulatory landscape, the legislative framework and potential future court proceedings that may arise in connection with misconduct considered by the Royal Commission.

In 2015, the federal government set an agenda for improving the Australian financial system in response to the findings of the Financial System Inquiry.³¹ In connection with this agenda, the government established the ASIC Enforcement Review Taskforce to review 'whether there is a need to strengthen ASIC's enforcement toolkit and if so, what that might look like'.³²

30 *Concut Pty Ltd v. Worrell* [2000] HCA 64, [23].

31 See D Murray et al, 'Financial System Inquiry: Final Report' (November 2014).

32 Minister for Revenue and Financial Services, Media Release: ASIC Enforcement Review Taskforce (19 October 2016), the Treasury, <http://kmo.ministers.treasury.gov.au/media-release/095-2016>.

In December 2017, the Taskforce released its report, which included 50 recommendations. On 16 April 2018, the government responded to the report and noted that it agreed, or agreed in principle, with all of the recommendations.³³ A further media release on 20 April 2018 announced an intention to prioritise 30 of the recommendations that would see significant increases to ASIC's powers. The remaining 20 recommendations will be considered alongside the final Royal Commission report.³⁴

ASIC is involved in ongoing litigation with a number of banks, and more proceedings are expected with many investigations underway. In its report on enforcement outcomes for the second half of 2017, ASIC noted that, over the next six months, it would have a particular focus on, among other things, responsible lending practices in the consumer credit industry, financial advisers' compliance with the best interests duty and their obligation to provide appropriate advice to clients and financial services licensees' failure to deliver ongoing advice services to financial advice customers who are paying fees to receive those services.³⁵ In 2017, Australia's competition regulator, the Australian Competition and Consumer Commission (ACCC), established a permanent Financial Services Unit (FSU) to monitor and promote competition in Australia's financial services sector by assessing competition issues, undertaking market studies and reporting regularly on emerging issues and trends in the sector. The FSU's first task was the Residential Mortgage Price Inquiry. An interim report, released in March 2018, identified signs of less-than-vigorous price competition, especially between the big four banks and a final report is due later in 2018.³⁶ It is not yet clear what litigation may follow the release of the final report.

In May 2018, APRA released the final report of its prudential inquiry into CBA.³⁷ The Prudential Inquiry was announced in August 2017 to examine governance, culture and accountability issues within the CBA group. The report identified a number of shortcomings in CBA's governance, culture and accountability frameworks, particularly in dealing with non-financial risks, and made recommendations to strengthen these frameworks. On releasing the report, APRA noted that all regulated financial institutions would benefit from conducting a self-assessment to gauge whether similar issues might exist in their institutions and it would expect institutions to be able to demonstrate how they have considered the issues within the report.³⁸

With Australian financial institutions coming under significant scrutiny as a result of the Royal Commission, Australia can expect private litigants (including litigants funded by litigation funders) to continue to focus their attention on the potential wrongdoing of financial institutions.

33 Australian government response to the ASIC Enforcement Review Taskforce Report (16 April 2018), <https://static.treasury.gov.au/uploads/sites/1/2018/04/Aus-Gov-response-ASIC-Enforcement-Review-Taskforce-Report.pdf>.

34 Minister for Revenue and Financial Services, Media Release: Boosting penalties to protect Australian consumers from corporate and financial misconduct (20 April 2018), <http://kmo.ministers.treasury.gov.au/media-release/039-2018/>.

35 See ASIC, 'ASIC enforcement outcomes: July to December 2017' (Report 568, February 2018).

36 See ACCC, 'Residential mortgage price inquiry: interim report' (March 2018).

37 See APRA, 'Prudential Inquiry into the Commonwealth Bank of Australia' (April 2018).

38 APRA, Media Release 'APRA releases CBA Prudential Inquiry Final Report and accepts Enforceable Undertaking from CBA' (1 May 2018), www.apra.gov.au/media-centre/media-releases/apra-releases-cba-prudential-inquiry-final-report-accepts-eu.

X LOOKING AHEAD

Banking litigation in Australia most commonly arises in relation to regulators and consumers, rather than between financial institutions themselves, which are seen to enjoy more equal bargaining power and may be more motivated to reach confidential settlements than pursue dispute resolution through the courts. Current increased regulatory and public scrutiny on banks contributes to an environment that is more susceptible to litigation. In light of the increased scrutiny as a result of the Royal Commission, as well as Australia's active class-action environment, the banking sector in Australia is likely to remain an active area for disputes for quite some time.

AUSTRIA

Holger Bielez, Paul Krepil and Florian Horak¹

I SIGNIFICANT RECENT CASES

The following noteworthy cases have recently been dealt with by the Austrian courts.

i Decision of the Austrian Constitutional Court upholding haircut on creditors of the nationalised bank, HETA Asset Resolution AG, secured by a provincial guarantee

In March 2018, the Austrian Constitutional Court confirmed a federal legislative act (Section 2(a) of the Financial Market Stability Act),² which had laid the ground for a general settlement offer proposed to the holders of outstanding claims against the former Hypo Alpe Adria banking group in autumn 2016 totalling claims of approximately €11 billion. The bank was subsequently nationalised under the name of HETA Asset Resolution AG (HETA) and is currently being liquidated under the bank recovery and resolution directive regime.³ The claims were secured by a statutory guarantee of the Austrian province of Carinthia and reached levels that were claimed by many politicians as endangering the economic survival of the province. The settlement offer was widely accepted by the creditors given the uncertainties of litigation against HETA and the province of Carinthia. Several holdout creditors challenged the underlying act before the Austrian Constitutional Court based on several breaches of the fundamental right to property and non-discrimination.⁴ However, the Constitutional Court confirmed the act thus providing backing to the proponents of the haircut. Currently, several civil lawsuits filed by holdout creditors are pending.

1 Holger Bielez is a partner, Paul Krepil is an associate and Florian Horak is a consultant, at Wolf Theiss.
2 Financial Market Stability Act, Official Gazette (BGBl) No. I 136/2008 as amended by Official Gazette (BGBl) No. I 127/2015.
3 Directive 2014/59/EU of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms, OJ 2014 L 173/190. The Directive was implemented by way of the Federal Act regarding the restructuring and liquidation of banks (BaSAG.), Official Gazette (BGBl) No. I 98/2014.
4 Constitutional Court decision dated 14 March 2018, G248/2017 et al.

ii Notifications to customers via e-banking: decision of the European Court of Justice of 25 January 2017⁵ and of the Austrian Supreme Court of 28 September 2017⁶

In this case, the Austrian Consumer Association (VKI) filed a representative action against an Austrian bank concerning a clause in the bank's general terms regarding notifications to customers via e-banking.

The respective section in the credit institution's standard general terms set forth that notices and statements (in particular account information, account statements, credit card statements and notices of changes) that the bank has to transmit to its customers or make available to them shall, where a customer has agreed to e-banking, be received by him or her by post, electronically (by making them retrievable) or transmitting them by means of e-banking.

Subsequently, the Supreme Court had to set up criteria under which notifications via e-banking may be considered as communicated on a 'durable medium'.⁷ As in the Supreme Court's view, this was a question of interpretation of Article 41, Paragraph 1 and Article 44, Paragraph 1 of Directive 2007/64/EC on payment services in the internal market.⁸ The Court presented the case to the European Court of Justice (ECJ) for a preliminary ruling.

The ECJ ruled that two conditions have to be met in order to fulfil the required standards:

- a* the (e-banking) website has to allow the user to store information addressed to him or her personally in such a way that he or she may access it and reproduce it unchanged for an adequate period, without any unilateral modification of its content by that service provider or by another professional being possible; and
- b* if the payment service user is obliged to consult that website in order to become aware of that information, the transmission of that information is accompanied by active behaviour on the part of the provider aimed at drawing the user's attention to the existence and availability of the information on the website.

In summary, if a credit institution wants to transmit information via e-banking, the bank has to make sure that the information transmitted is made available at any time for a reasonable period of time. Further, the bank has to draw the customer's attention to the existence and availability of the information on the website, otherwise it may not rely on the information afterwards. In other words, the bank must actively inform the customer that there is information deposited in the e-banking system. On 28 September 2017, the Supreme Court eventually rendered its decision. Based on the preliminary ruling by the ECJ, the litigious clause was found impermissible.

5 EuGH 25 January 2017, C-375/15.

6 OGH 28 September 2017, 8 Ob 14/17t.

7 Durable medium means any instrument that enables the payment service user to store information addressed personally to him or her in a way that is accessible for future reference for a period of time adequate to the purposes of the information, and that allows the unchanged reproduction of the information stored.

8 The Austrian Payment Services Act (ZaDiG), which implemented Directive 2007/64/EC, foresees information and notices by the credit institution to be provided either in paper or through another durable medium (Section 26, Paragraph 1, No. 1; Section 29, Paragraph 1, No. 1 ZaDiG);

iii Negative interest: decision of the Supreme Court of 21 March 2017⁹

This decision was triggered by way of a representative action for injunctive relief filed by the VKI against an Austrian bank. The credit institution had entered into foreign currency loan agreements – in this case Swiss francs – with consumers. The interest rate consisted of a fixed rate and a variable interest rate that was linked to the London Interbank Offered Rate (LIBOR). In 2014, the Swiss franc LIBOR rate became negative. This posed the risk that the total interest rate due (including the agreed fixed rate) would become negative. Consequently, the Austrian bank announced that it would freeze the interest rate at zero per cent in that scenario. The bank, however, did not intend to pay negative interest to its customers.

In its decision the Supreme Court set forth that loan agreements by their nature are agreements in return of payment. A loan agreement is a contract in which a bank arranges to lend a customer a certain amount of money for a specified amount of time. In return the customer must pay a certain interest rate to the credit institution. For that reason, it contradicts the nature of the contract if the creditor becomes obligated to pay interest to the credit user for providing the agreed amount. In the Court's view this would also be covered by the parties' will. Under normal circumstances no credit user would expect to receive interest for being provided with a loan. Consequently, the Supreme Court dismissed the representative action by the VKI. It pointed out, however, that in some cases the parties might agree on an interest rate agreement that could foresee an obligation for the creditor to pay negative interest. Such an interpretation would depend on the case. The Court took a similar approach in a case in April 2017.¹⁰

iv Negative interest: decision of the Supreme Court of 3 May 2017¹¹

In this recent decision of the Supreme Court, the financial institution argued that the customer would at least have to pay the fixed rate if the variable rates became negative (in this case the consumer entered into two credit agreements). The Supreme Court ruled that the wording of the credit agreement was sufficiently accurate and consequently there would be no possibility of coming to a conclusion as claimed by the bank (in the Court's view the legal question was a question of interpretation of the credit agreement). Further, the bank's argument contradicted provisions implemented in the Austrian Consumer Protection Act (ACPA) (see Section 6, Paragraph, 1, No. 5).¹² Therefore, a creditor cannot, in fact, be compelled to pay negative interest to a credit user. A credit user, on the other hand, is – at least concerning this case – not obliged to pay the fixed rate in case of a negative variable rate. The outcome of this case may lead to recovery claims of customers against banks that used to charge at least the fixed rate even in times of negative interest rates.

v Negative interest: further decisions by the Supreme Court

The Supreme Court confirmed its approach in its decision of 30 May 2017,¹³ which was based on a representative action by the VKI.

9 OGH 21 March 2017, 10 Ob 13/17k.

10 OGH 26 April 2017, 1 Ob 4/17w.

11 OGH 3 May 2017, 4 Ob 60/17b.

12 Koch, 'Negative interest: no minimum entitlement according to a fixed rate through interpretation of the contract', *ÖBA* 2017, p. 422.

13 OGH 30 May 2017, 8 Ob 101/16k.

Subsequently, further decisions were rendered on 13 June 2017,¹⁴ 28 June 2017,¹⁵ 29 August 2017¹⁶ and 30 August 2017,¹⁷ confirming the Supreme Court's prevailing opinion on this topic. The legal situation on negative interests seems now to be sufficiently clarified. A different approach is, thus, not to be expected in the near future. Owing to the referenced case law, comparable cases would not yet constitute a significant legal issue that sets a precondition for access to the Supreme Court. However, all of the aforementioned decisions concern claims filed on behalf of consumers versus banks. There does not seem to be any case law on disputes initiated by corporate customers and the existing case law cannot automatically be applied to cases outside of business-to-business relationships.

vi Case law regarding the international jurisdiction of EU Member State's courts for consumer claims based on prospectus liability and related claims

In July 2017, the Supreme Court issued a decision on the international jurisdiction of the Austrian courts for damage claims owing to investments in certain capital market products. *Inter alia*, the court decision deals with the difficulties identifying 'the place of the damaging event' for the purposes of Article 7(2) of the Brussels Ia Regulation¹⁸ in cases of pure monetary damages. The Supreme Court held that, in cases of prospectus liability claims, the place of the damaging event is the place where the wrongful information in the prospectus was published. In the case at hand it remained open, whether a notification of a prospectus into another EU Member State ('passporting') would have any impact on the determination of the place of the damaging event. Further, the court held that the place of the occurrence of the damage was not located in Austria either, because the plaintiff had purchased the financial instruments in Germany, which is also where the global certificate was deposited. The Court did not have to deal with the difficult questions of identifying the place of the damaging event in cases of international money transfers financing the harmful investment because there were no such money transfers in the case at issue. Particularly with respect to such money transfers and whether they provide claimants a place of jurisdiction based on Article 7(2) of the Brussels Ia Regulation typically close to their home country, the ECJ has not yet found satisfactory solutions.¹⁹ Currently, another preliminary ruling is pending with the ECJ under case C-304/17 (*Löber*),²⁰ which may help clarify the current uncertainties.

14 OGH 13 June 2017, 4 Ob 107/17i.

15 OGH 28 June 2017, 9 Ob 35/17p.

16 OGH 29 August 2017, 6 Ob 51/17v.

17 OGH 30 August 2017, 3 Ob 88/17p.

18 Regulation (EU) No. 1215/2012 of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, OJ 2012 L 351/1.

19 The relevant existing cases decided by the ECJ are C-168/02 (*Kronhofer*), ECLI:EU:C:2004:364; C-375/13 (*Kolassa*), ECLI:EU:C:2015:37; and C-12/15 (*Universal Music Holding v. Schilling et al*) ECLI:EU:C:2016:449.

20 OJ 2017 C 269/6. The opinion of the Advocate General is already available (ECLI:EU:C:2018:310).

II RECENT LEGISLATIVE DEVELOPMENTS

i Beneficial Owner Register Act

The Beneficial Owner Register Act (BORA) was introduced in Austria by way of implementation of Articles 30 and 31 of Directive (EU) 2015/849²¹ into national law and provides for a register of ultimate beneficial owners (UBOs) of all legal entities listed in Section 1 of the BORA (see below).²² Reportable entities must notify their beneficial owners to a register, observe various due diligence requirements and, in the case of violations, face strict sanctions. The register aims to support those professional groups that are subject to stringent anti-money laundering and terrorist financing rules (i.e., financial institutions).²³ The BORA entered into force on 15 January 2018.

Reportable entities

In general, all relevant company structures with their registered seat in Austria are required to register their UBO. Reportable entities include unlimited liability partnerships, limited liability partnerships, limited liability companies, public limited companies and *societas Europaea*, etc. In addition, trusts managed in Austria and trust-like agreements are also included.

UBOs

UBOs are all natural persons who own or control a registering entity (irrespective of the domicile of such entity). UBOs can be divided into three groups (capital ownership percentage, voting interest and factual control) on the basis of which ownership and control is determined. In general, the Act distinguishes between three types of economic owners:

- a direct economic owners: these are natural persons who:
- hold 25 per cent plus one share, or more than a 25 per cent participation of the registering entity or the respective votes; or
 - exercise control over the management of the registering entity, whereby ‘control’ is defined as holding – either directly or indirectly – 50 per cent in shares plus one share, or more than a 50 per cent participation of the registering entity or the respective votes. Control is further assumed under the circumstances applicable for drawing up consolidated annual financial statements pursuant to Section 244, Paragraph 2 of the Austrian Enterprise Act;²⁴

21 Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.

22 Mainly, the entities listed in Section 1 of the BORA are registered with the Austrian Commercial Register.

23 Barbist/Gassner, ‘The new register for beneficial owners’, *Ecolex* 2017, p. 1170.

24 Section 244 of the Austrian Enterprise Act includes parent companies having in another company (subsidiary): (1) the majority of voting rights of shareholders; (2) the right to appoint or remove the majority of management or supervisory bodies, in the case the parent company is also a shareholder; (3) the right to exercise a controlling influence; or (4) the right to decide, on the basis of an agreement with shareholders of one or more subsidiaries, comparable to voting rights of a shareholder, on the appointment or revocation of the majority of the administrative, management or supervisory body.

- b* indirect economic owners as UBOs: these are natural persons who ‘control’ (see above) an entity that directly or indirectly holds 25 per cent plus one share, or more than a 25 per cent participation in the registering entity or the respective votes. If more than one registering entity is controlled by the same natural person or the same natural persons, either directly or indirectly, and cumulatively exceed the thresholds of 25 per cent plus one share, or more than a 25 per cent participation in another entity, then such natural person shall be regarded as the economic owner of such entity; and
- c* *ex lege* economic owner: if no economic owner can be determined according to the above framework (i.e., the top entity is a listed company with widely held stock), the management of the registering entity is determined as the UBO by operation of law.²⁵

Special provisions apply for partnerships, cooperatives, (foreign) trusts and foundations.

Exceptions

In certain cases, exceptions from mandatory registration apply. This is the case for partnerships and limited liability companies, for example, if the personally liable direct partners or shareholders consist only of natural persons and, thus, the relevant data for the register can easily be taken from the commercial register. However, these exemptions only apply if no person other than the legally registered person exercises direct or indirect control over the management of the legal entity.

Due diligence

According to Section 3 of the BORA, an entity subject to mandatory registration has to ascertain and verify the identity of its ultimate beneficial owners at least once a year. Therefore, there is the requirement for entities to undertake regular investigations and to store the relevant corresponding documentation. In order to fulfil this due diligence duty, all necessary measures to understand the ownership and control structure need to be taken by the registering entity. As indicated above, the UBO can, in any case, only be a natural person.²⁶

Right to inspect the register

Unlike the commercial register, the UBO register is not publicly available. Section 9 of the BORA provides for a list of entities that are granted a right to inspection. Besides certain authorities, this list, *inter alia*, includes the following persons and organisations: financial institutions, attorneys at law and public notaries. However, inspections are only permissible in the context of applying due diligence to prevent money laundering and terrorist financing in relation to customers or to advise clients on the identification, verification and reporting of their UBOs.

25 See Section 2, Paragraph 1(b) BORA.

26 Kühne, “The determination of the beneficial owner according to the Beneficial Owner Register Act”, *Ecollex* 2018, p. 205.

Sanctions

Violations of the mandatory registration or incorrect reports are considered financial offences and can lead to a fine of up to €200,000 (for intent) or €100,000 (for gross negligence). For unauthorised inspections of the register, a fine of up to €100,000 may be imposed in the case of deliberate conduct.

Deadline for registration

Initial filings have to be made before 15 August 2018. This deadline, originally proclaimed for 1 June 2018, was extended by decree of the Federal Ministry of Finance owing to the high number of registrations.

ii The Financial Market Money Laundering Act

By way of the Financial Market Money Laundering Act (FMMLA), Austria implemented Directive (EU) 2015/849 (see Section II.i, above). The new legislation entered into force on 1 January 2017 and introduced consolidation of money laundering provisions for banks in Austria (which can now mainly be found in the FMMLA). Several innovations were included,²⁷ as outlined below.

Enhancement of the risk-based approach

According to the new Act, the risks of money laundering and terrorist financing, as well as data protection problems, must be detected, analysed and reduced. The mandatory risk assessment has to be recorded and updated regularly, and must take place on a national level,²⁸ as well as on a company level (i.e., for obligated institutions; see Section 4 of the FMMLA).²⁹

Online identification

As previously implemented in the Austrian Banking Act and the Austrian Insurance Supervision Act, the FMMLA provides for provisions on due diligence on customers. Financial institutions are required to obtain and hold adequate, accurate and current information on the beneficial ownership of their customers, including the details of the beneficial interests held, their customers' identity, the purpose of the intended business relationship, the origin of funds and the identity of possible trustees. In general, natural persons have to prove their identity by means of official photo identification. However, according to new provisions in the FMMLA, online identification (using video-supported technology) is possible in cases where – within the scope of the normal customer due diligence provisions – the risk can be considered minor because the customer is not present.³⁰ The general scope of due diligence provisions has, however, remained unchanged.

Enhanced customer due diligence measures in respect of politically exposed persons

According to the new Article 11 of the FMMLA, a higher standard for due diligence measures is applicable with regard to persons who are politically exposed. In addition to the above-mentioned principles on due diligence (Article 6 of the FMMLA), credit and

27 Durstberger/Nicolussi, 'FMMLA passed', *GesRZ* 2017, p. 3.

28 In Austria, the competent authority is the Finance Minister (see Section 3 FMMLA).

29 Ruhm/Tutsch, 'Current legislation on the financial market', *ZFR* 2017, p. 100.

30 Id.

financial institutions have to implement appropriate risk management systems to determine (1) whether a politically exposed person is involved in a business relationship with the institution, and (2) the origin of funds that are involved in transactions or throughout the business relationship. Further continuous monitoring of the business relationship is required and the management of the financial institution has to give its consent prior to the involvement of a politically exposed person.

Harsher penalties for financial institutions

The FMMLA foresees administrative penalties by the Austrian Financial Market Authority (Article 35 of the FMMLA) of up to €5 million or 10 per cent of the financial institution's yearly turnover. However, the essential penalty depends on the severity of the infringement. Owing to the principle of proportionality, the Authority may also entirely refrain from imposing a penalty (see Section 35, Paragraph 4 of the FMMLA).³¹

In June 2018, the Fifth Money Laundering Directive,³² amending Directive (EU) 2015/849, was enacted, and this must be implemented by EU Member States by 10 January 2020. In essence, the new Directive aims to increase transparency for e-money products by way of (1) reduced thresholds requiring customer identification and stricter KYC rules; (2) bringing virtual currency platforms into the scope of Directive (EU) 2015/849; (3) increased duties of care towards high-risk countries; (4) expansion of the competencies of financial intelligence units and improvement of their cooperation; and (5) increased transparency regarding beneficial owners.

iii Possible class action provisions

It seems that the Ministry of Justice has abandoned its plans to implement real class action provisions in Austria.³³ In contrast, the European Commission presented a draft proposal for its 'New Deal for Consumers' in April 2018, aiming to strengthen citizens' rights by allowing the filing of class-action suits. The European Commission is working on rules for two categories of lawsuits: one for situations in which a limited group of people suffered comparable harm and would collectively sue the defendant; and the other for low-value cases in which many consumers only suffered a small loss. In the latter case, the benefit would go to a public cause benefiting consumers. Separately, the European Union is proposing harsh fines of up to 4 per cent of a company's annual turnover for firms found guilty of widespread infringements. The latest initiative of the European Commission is perceived as a consequence of the diesel scandal, which may not – according to some – be adequately addressed within the European Union.³⁴

31 In addition, the FMMLA foresees penalties for violations of responsible representatives (see Section 34 FMMLA).

32 Directive (EU) 2018/843; OJ 2018 L 156/43.

33 www.ots.at/presseaussendung/OTS_20171124_OTS0028/liste-pilzkolba-vw-geschaedigte-brauchen-rasch-die-sammelklage (last visited on 26 June 2018).

34 Id.

III INTERIM MEASURES

i General

In Austria, it is possible to request a preliminary injunction to secure a monetary claim in cases of subjective endangerment in the course of pending civil proceedings or before filing a claim. The relevant provisions are regulated within the Austrian Enforcement Act (AEA).³⁵ The precondition for such a preliminary injunction is the existence of subjective endangerment respective to the recovery of the claim. A case of subjective endangerment may be argued successfully if it is obvious that without a preliminary injunction the opposing (and likely to be liable) party will make it difficult for the other party to pursue its claim, for example, by damaging, destroying, hiding or moving away assets³⁶ (see Section 379, Paragraph 2, No. 1 of the AEA).

With regard to banking litigation, the abusive demand of bank guarantees is a very common ground to file a request for a preliminary injunction. In such cases, the bank, which issued the guarantee, is prohibited from paying a debt to the opposing party by court order. If a bank violates the court order, it becomes liable for damages.³⁷ To secure monetary claims, the court is limited to specific measures depending on the respective object. The following measures are regulated in the AEA (Section 379, Paragraph 3):

- a A prohibition addressed to third-party debtors not to pay a debt to the opposing party. This is a frequently used method to secure funds. For example, the bank holding an account for the opposing party is prohibited by way of court order to make any payment upon the opposing party's instruction or to make payments owing to an abusive demand of a bank guarantee.
- b Movable objects including money: if it is possible to put the object into judicial custody, or administration or management, the court may further render an order to the opposing party to refrain from giving away, selling or pawning the movable object.
- c Immovable objects: if it is possible to put the object into judicial custody, or administration or management, the court may further render an order to the opposing party to refrain from giving away, selling, hypothecating or registering any encumbrances in the Land Register.

ii Cross-border interim measures

It is also possible to enforce an external freezing order or an injunction in Austria. The enforceability and recognition of an external freezing order depends on whether the court decision was rendered in an EU Member State or in a non-EU or foreign country.

EU Member States

In general, the regime of the Brussels Ia Regulation³⁸ is also applicable to freezing orders and requests for interim measures, such as injunctive relief. As a result, freezing orders and injunctive relief by another Member State's court are automatically recognised and enforceable in Austria without any further procedure on recognition required.³⁹ However,

35 RGBI 1896/79, in its applicable version.

36 Kodek in Angst/Oberhammer, EO3, Section 379, AEA, Paragraph 7ff.

37 Kodek in Angst/Oberhammer, EO3, Section 379, AEA, Paragraph 34.

38 Regulation (EU) No. 1215/2012 of the European Parliament and of the Council of 12 December 2012.

39 Thomas Garber in Angst/Oberhammer, EO3, Section 79, AEA, Paragraph 11.

since recognition and enforcement can be rejected by other EU Member States if the opponent was not granted a hearing – *ex parte* injunctions are frequently not recognised and enforced – only those freezing orders and injunctions where the defendant has been granted a hearing in the Member State of origin can subsequently be recognised and enforced in another Member State.

With regard to bank accounts within the European Union (except Denmark and the United Kingdom), Regulation (EU) No. 655/2014⁴⁰ establishes a European Account Preservation Order procedure to facilitate cross-border debt recovery in civil and commercial matters.

Foreign/non-EU countries

Freezing orders and interim injunctions that have been rendered in a foreign country outside the European Economic Area (EEA) are enforceable in case bilateral or international treaties are in place, which foresee mutual recognition and enforcement. In principle, freezing orders or interim injunctions must be declared enforceable. The following general requirements for the issuance of a declaration of enforceability are set forth in Section 406 of the AEA:⁴¹ (1) a foreign judgment is enforceable in the state in which it was rendered; and (2) reciprocity with the state of origin is established by way of bilateral treaties or other instruments (actual reciprocity by way of judicial ‘practice’ does not suffice).

The party seeking to receive the declaration of enforceability needs to file such request to the competent Austrian court. According to the AEA the district court of the opposing party’s domicile has jurisdiction. In addition, the party is required to enclose certified copies of all relevant documents with such request. The application for enforcement may be combined with the request.

- According to Section 408 of the AEA, the declaration of enforceability may be refused if:
- a* pursuant to Austrian rules on jurisdiction, the foreign court could not, under any circumstances, have jurisdiction over the legal matter;
 - b* the opposing party was not properly served with the document that initiated the foreign proceeding;
 - c* the opposing party could not properly participate in the foreign proceeding owing to irregularities in the proceeding; or
 - d* the judgment violates basic principles of Austrian public policy.

In practice, interim relief is typically sought before the Austrian courts if Austrian assets will be secured. This is because most of the creditors want to make use of the surprise effect of *ex parte* injunctions, which are not recognised or enforceable if issued by a foreign court, since the defendant is not granted a prior hearing. Applications for enforcement of injunctions from non-EEA countries in Austria are extremely rare.

iii Procedure in Austria

With the request for a preliminary injunction, the applicant must provide available evidence, such as documentary evidence and affidavits that can be immediately examined by the court. Foreign-language documents should be presented with German translations. Generally, a

40 Regulation (EU) No. 655/2014 of the European Parliament and of the Council of 15 May 2014.

41 Before 1 December 2016, the respective provisions were included in Section 79, AEA.

decision on a request for a preliminary injunction is rendered within a seven-week period. Regarding appellate proceedings, a time frame of one to three months for the second instance proceeding and a further two to four months in third instance proceedings has to be expected.

IV LAWYER–CLIENT PRIVILEGE

Section 9, Paragraph 2 of the Austrian Lawyers Act (ALA) sets forth the lawyer’s duty of confidentiality regarding all matters that were disclosed to him or her in his or her function as counsel whose non-disclosure is in the interest of the client. Therefore, a lawyer has the right to deny testifying in court or before any other authority according to the respective procedural provisions. Section 9, Paragraph 3 of the ALA prohibits circumventing this principle by, for example, interrogation of employees of the lawyer or seizing communications. The procedural implementation of these principles has led to several not entirely identical provisions in the various codes of procedure.⁴²

Regarding criminal proceedings, the attorney’s right to deny testifying as a witness is stated in Section 157 of the Austrian Code of Criminal Proceedings (ACCP).⁴³ As mentioned above, owing to the prohibition on circumventing, seizing communications between attorneys and defendants is also prohibited. An amendment of the provision means that this is now also applicable in cases where these communications are located outside the attorney’s office (e.g., at the defendant’s apartment). However, there is the requirement that all documents and data must have been created either by the attorney or the defendant. Documents that have been created by another person (e.g., a legal expert) and later handed to the defendant or the attorney do not fall within the provision.

In addition to those already mentioned, similar provisions can be found in: Section 321 of the Code of Civil Procedure, Sections 89 and 104 of the Finance Criminal Code, Section 49 of the Code of Administrative Procedure and Sections 171 and 143 of the Austrian Fiscal Code.

V JURISDICTION AND CONFLICTS OF LAW

There are, generally speaking, no specific rules on jurisdiction and conflicts of law regarding banking institutions, therefore the general rules set forth below apply.

i Domestic rules on jurisdiction

The Austrian judicial system differentiates between local jurisdiction and competence of the courts. The competence of a court mainly depends on the amount in dispute. District courts are the first instance to decide in civil law cases with a maximum amount in dispute of €15,000. In addition, the district courts have competence irrespective of the amount in dispute on certain types of cases, for example, family and rent law cases. Regional courts as courts of first instance are responsible for rulings in all matters not assigned to district courts.

42 Prunbauer-Glaser, “Legal Professional Privilege” v. Schutz der anwaltlichen Verschwiegenheit, *AnwBl* 2013, p. 56.

43 Owing to the implementation of Directive 2013/48/EU, an amendment of Section 157 of the ACCP entered into force on 1 November 2016.

In the Austrian Court Jurisdiction Act,⁴⁴ there are several provisions regulating jurisdiction. As a basic principle, the court at the defendant's place of residence has jurisdiction. For consumer-based claims, the ACPA⁴⁵ also stipulates that according to the basic principle on jurisdiction, the court at the defendant's place of residence has jurisdiction. Consumer-based claims are matters relating to a contract concluded by a person for a purpose that can be regarded as being outside his or her trade or profession.

According to Section 104 of the Austrian Court Jurisdiction Act, for non-consumer based claims, the parties may agree on a forum clause. The forum clause has to be in writing and to be valid it must specify a specific litigation or any legal dispute that may arise from a specific contractual relationship. Choices of forum clauses for consumer-based claims that violate the special jurisdiction for consumer-based claims are null and void.

ii International jurisdiction

International jurisdiction – except where the defendant is not domiciled within the EU (see Article 6 of the Brussels Ia Regulation) – is regulated by the Brussels Ia Regulation. According to the Regulation, in principle, the court of the Member State of the defendant has jurisdiction.

Article 7 of the Brussels Ia Regulation constitutes a supplement to the general principle of jurisdiction. In matters relating to a contract, a person domiciled in a Member State can be sued in the courts of the place of performance of the obligation in question (Article 7, Paragraph 1a). In matters relating to tort, delict or quasi-delict, a person domiciled in a Member State can be sued in the courts for the place where the harmful event occurred or may occur (Article 7, Paragraph 3). This is deemed to also include the place where the damage occurred. In other words, a forum can be established both in the place where the event triggering the damage took place and the place where the damage actually occurred. The provision plays a crucial role with regard to cross-border banking disputes as it enables claimants to sue a bank in their home jurisdiction, provided that the place of performance or the place of the damaging event is there. However, the provision regularly gives rise to interpretation issues, which lead to disputes on jurisdiction and may prolong the dispute.

According to Article 25 of the Brussels Ia Regulation, the parties of a contract may agree on the jurisdiction of a court of a Member State. There does not have to be a connection between the parties and the forum. Unless agreed otherwise, the chosen forum has exclusive jurisdiction. A choice of forum clause must fulfil one of the following conditions to be valid:

- a* the forum clause must be in writing or evidenced in writing;
- b* the choice of forum is according to practices that the parties have established between themselves; or
- c* the choice of forum is according to international commercial customs.

Last but not least, the rules on consumer jurisdiction pursuant to Articles 17 and 18 of the Brussels Ia Regulation must be borne in mind in particular with respect to banking disputes. Generally, the provisions allow for consumers to sue their counterparty both at the place of their domicile or at the defendant's domicile. However, lawsuits filed by the consumer's counterparty may only be filed at the consumer's domicile.

44 RGBI, No. 111/1895, in its applicable version.

45 BGBl, No. 140/1979, in its applicable version.

iii Conflicts of law

In Austria, conflicts of law are generally regulated by the International Private Law Act.⁴⁶ Further, in relation to contractual obligations, the Rome I Regulation⁴⁷ is relevant and regards non-contractual obligations in the Rome II Regulation⁴⁸ (including obligations derived from *culpa in contrahendo*).

In principle, the parties, both in business-to-business and business-to-consumer contracts, are free to choose the applicable law. Failing a choice of law, the Rome I Regulation provides that depending on the circumstances, either the law of the place where the service provider is resident applies or the law of the party that performs the characteristic obligation applies (Article 4 of the Rome I Regulation). More complex rules apply to international consumer contracts. Pursuant to Section 13a of the ACPA, certain sets of rules cannot be altered by way of a choice of law, if the choice of law leads to the application of the law of a non-EEA Member State (Paragraph 1). In addition, the Austrian law provisions governing the application and validity of general terms and conditions of a consumer contract are mandatory in all cases where the consumer contract was concluded because the counterparty expanded its commercial activity to Austria, and the consumer contract was concluded as a result of such activity (Paragraph 2). This means that the general terms and conditions of any foreign bank directing its retail business to Austria must comply with the mandatory Austrian rules governing application and validity of such general terms and conditions.

The Rome I Regulation also allows the courts of the Member States to apply ‘its overriding mandatory’ rules, irrespective of which law applies to the contract (Article 9 of the Rome I Regulation).

The application of foreign law has to be established *ex officio*. In such cases, the court that has to apply foreign law will consult with the Austrian Ministry of Justice and has to rely on expert opinions. If foreign law cannot be established within a stipulated time frame despite considerable efforts, Austrian law will be applied.

VI SOURCES OF LITIGATION

Banking litigation in recent years has revealed that banks are more likely to be defendants in lawsuits than plaintiffs. Nevertheless, a few cases with high amounts in dispute were initiated by banks, for example, a case filed by a well-established Austrian bank against an Austrian community seeking redress for the closing costs of derivative instruments with negative market value, which had been purchased by the public administration in order to improve its debt management.

With regard to banks as defendants, numerous cases were triggered following the start of the financial crisis in 2008, which concerned alleged breaches of advisory duties in the context of the marketing and sale of certificates. These included claims based on prospectus liability if the bank was involved in the issuance or control of prospectus information. These cases reached four-digit sums at various Austrian courts and were responsible for a significant statistical increase in lawyers’ caseloads.

⁴⁶ BGBl No. 304/1978, in its applicable version.

⁴⁷ Regulation (EC) No. 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I), OJ 2008, L 177, p. 6.

⁴⁸ Regulation (EC) No. 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (Rome II), OJ 2007, L 199, p. 40.

Such cases are now in decline as they are being resolved by way of final judgment or settlement. However, nowadays banks seem to be increasingly exposed to representative actions filed by consumer protection associations, primarily the VKI, seeking the removal of terms and conditions used by banks for alleged non-compliance with transparency and *contra bonos mores* rules, as provided for in Austrian consumer law. The most recent example is the issue of negative interest loan agreements (including FX loans), which focuses on the extent to which banks are obliged to pass on the economic benefit of negative interest in loan arrangements to the customer.

VII EXCLUSION OF LIABILITY

According to Austrian law, a total exclusion of liability is prohibited. Provisions to that effect are therefore null and void. Consequently, exclusion of liability for intentional or conscious violations is not possible. Whether this also applies for certain cases of gross negligence is often discussed by scholars. Generally, exclusion of liability for gross negligence is – even though there are some exceptions – not permissible. Exclusion of liability for slight negligence is largely permissible,⁴⁹ but not for personal injury.⁵⁰

The ACPA provides for exclusion of liability in consumer contracts. For other damages (e.g., financial loss) exclusion of liability is not possible for gross negligence and intentional damages according to the ACPA.⁵¹ Moreover, any contractual provision included in the general terms and conditions or contractual form shall be ineffective if it is unclear or unintelligible.

Regarding gross negligence, the Supreme Court distinguishes between gross negligence and extreme gross negligence, which implies conduct that cannot be expected on the basis of usual daily life experience. According to the Supreme Court, exclusion of liability for extreme gross negligence contradicts good manners and is therefore considered equal to intentional damaging conduct. Thus, exclusion of liability for extreme gross negligence is prohibited in any case. Agreements that exclude liability for extreme gross negligence are therefore null and void. The circumstances in which conduct can be considered grossly negligent or extremely grossly negligent constitutes a difficult normative question that, to a great extent, depends on the facts of each case.⁵²

i Credit reports

Regarding credit reports, the Supreme Court ruled (7 Ob 666/84)⁵³ that exclusion of liability for gross negligence – but not for extreme gross negligence – was justified and valid owing to the fact that companies could largely pass on their general business risks (i.e., their relevant credit risk (owing to the insolvency of their customers) onto the financial or credit institutions.⁵⁴ In

49 Krejci in Rummel/Lukas, ABGB4 Section 879, Civil Code, Paragraphs 122 to 130.

50 Reischauer in Rummel, ABGB3 Section 1298, Civil Code, Paragraph 10a.

51 Reischauer, 'Contractual exclusion of liability for culpable conduct, in particular gross negligence', *ÖJZ* 2009/114.

52 Krejci in Rummel/Lukas, ABGB4, Civil Code, Section 879, Paragraphs 122–130.

53 OGH 22 November 1984, 7 Ob 666/84; SZ 57/184; *EvBl* 1985/98 p. 495; *RdW* 1985, p. 73; *JBl* 1986, p. 168.

54 Reischauer, 'Contractual exclusion of liability for culpable conduct, in particular gross negligence', *ÖJZ* 2009/114.

the Supreme Court's view providing credit reports is a big business that has high risks as the conditions subject to the assessment are, in some cases, very complex. The Supreme Court argued that credit and financial institutions generally have little self-interest in this regard as they do not usually receive any compensation for providing such credit reports. Therefore, financial institutions have a legitimate interest in restricting their liability. For this reason, it seems possible to restrict liability to extremely grossly negligent and intentional conduct.

ii Consulting on funding opportunities

The Supreme Court's jurisprudence on exclusion of liability concerning credit reports is, however, not applicable with regard to consulting on funding opportunities in connection with the financing of a company. The specific issues in one underlying decision (6 Ob 541/92)⁵⁵ were whether exclusion of liability was permissible for miscounselling in connection with funding opportunities. In this respect, the Supreme Court argued that credit and financial institutions generally have self-interest in the conclusion of the business transaction especially when the consulting services are closely linked to credit accommodations.⁵⁶ Therefore, a legitimate interest to restrict one's liability is not predominant. For this reason, an exclusion of liability for grossly negligent conduct would be null and void.

VIII REGULATORY IMPACT

Generally, the increasing pressure applied to banks by the regulator makes financial institutions cautious as to whether they are ready to introduce new products of higher complexity. This conduct reduces the risk of getting exposed to litigation. Currently, financial institutions are still prioritising getting in line with constantly evolving regulatory requirements, regarding, for example, the updated anti-money laundering rules (see Section II.ii, above) and the changes incurred through the future implementation of the Markets in Financial Instrument Directive (MiFID) II.

At the same time, we expect the latest regulatory developments, such as MiFID II, to continue influencing the case law of the civil law courts. More so than before, breaches of the regulatory rules will be construed as breaches of contractual or pre-contractual duties enabling the customer to adapt or rescind a contract or seek damage compensation. Banks are therefore likely to continue focusing primarily on their internal processes, implementing the increased regulatory duties of care not only to avoid administrative sanctions, but also to reduce the risk of exposure in civil litigation.

IX LOOKING AHEAD

In the years following the 2008 financial crisis, banking litigation played a significant role before the Austrian courts, in particular in Vienna. In particular, damage claims filed by retail investors for wrongful advice or wrongful prospectus information were responsible for capacity restraints before the courts. The sheer number of these lawsuits and their complex nature contributed to the significance of these banking litigation cases in Austria after 2008.

55 OGH 11 June 1992, 6 Ob 541/92; ÖBA 1993, p. 325 (*Jabornegg*); *JBl* 1993, p. 397; *RdW* 1992, p. 399.

56 Reischauer, 'Contractual exclusion of liability for culpable conduct, in particular gross negligence', *ÖJZ* 2009/114.

Nowadays, such claims are in decline as many cases not yet filed with the court are under increased risk of being rejected as time-barred. This decline does not seem to have been compensated by new cases.

However, representative lawsuits filed by consumer associations (dealing with the application and validity of general terms and conditions towards banks' customers) will continue as the banks are under competitive pressure and cannot afford to relent, especially in cases where the dispute with the consumer organisation will have an impact on the income of the bank. The latest disputes regarding the 'negative interest' cases serve as an example. Further, we anticipate an increase in litigation cases against former management board members of financial institutions based on breaches of professional duties of care.

BELGIUM

Stefaan Loosveld¹

I RECENT LEGISLATIVE DEVELOPMENTS

i Changes to the Law of 2 August 2002

The Belgian Law of 2 August 2002 on the supervision of the financial sector and the financial services (the Law of 2 August 2002) contains a significant number of provisions that affect the relations between banks and their clients. The provisions relate to, among other things, the transposition in Belgian law of the original MiFID rules (MiFID I).² These rules set forth the duties of a bank when providing advisory or portfolio management services to clients (see Section VII, below, for the regulatory impact of the upcoming transposition in Belgium of the MiFID II rules).

In banking disputes, the general evidentiary rules under Belgian law apply as a rule. This means that each party needs to evidence the claims it makes and the defences it raises. Thus, a banking client who asserts contractual or tortious liability claims against a bank needs to show: (1) a breach of contract (contractual liability), or a breach of general duty of care, which includes the breach of a statutory provision (tortious liability); (2) the damage incurred by that client; and (3) the causal link between the breach and the damage. For instance, in disputes regarding discretionary portfolio management, clients often invoke one or more asserted breaches of the MiFID I rules as a basis for their civil claims.

Applicable with effect as of 9 September 2013, the Law of 2 August 2002 also contains a provision in its Article 30 *ter* that is unrelated to the MiFID I rules, and that aims to facilitate the burden of proof for investors in liability disputes. It sets forth that, if, at the occasion of a financial transaction, a bank breaches one or more specifically listed statutory rules (which include a number of MiFID I rules) and the client suffers damage because of this transaction, then the transaction is presumed to be the consequence of the breach. This presumption of a causal link between the breach and the transaction is rebuttable. It is without prejudice to the possibility for the client to invoke other rules, and cannot be contractually waived by the client. The practical usefulness of this presumption should, however, not be overrated. Indeed, it is not a presumption of a causal link between the breach and the damage incurred by the client, but only a presumption that the transaction results from the breach. The client still needs to evidence that the asserted damage was caused by the breach.

1 Stefaan Loosveld is a partner at Linklaters LLP. The information contained in this chapter is accurate as of August 2017.

2 Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC (OJ L 145, 30 April 2004, p. 1).

ii Legislation on class actions

Through two laws of 27 and 28 March 2014, a class action mechanism was introduced in Belgian law with effect from 1 September 2014.

A class action aims to offer reparation to consumers who have suffered a collective prejudice because of the breach by an undertaking of one of its contractual commitments or one of the European or Belgian law statutory rules that are specifically listed by law. These rules concern, among other things, competition law, market practices and consumer protection law, payment services, certain insurance contracts and certain provisions of the Law of 2 August 2002. The notion of 'collective prejudice' refers to all the damage that has a common cause and that has been suffered by the members of the group. The purpose of the class action is to ensure that connected questions of fact and law are treated in the same procedure, with both opt-in and opt-out features. The handling of class action proceedings has been centralised for the entire Belgian territory within the jurisdiction of the Brussels courts.

While a class action might also be initiated against a bank because of certain practices and activities of the bank, a class action is only open to consumers. A consumer is an individual (physical person) who acts for a purpose that does not enter within his or her commercial, industrial or professional activities. The notion of 'consumer' for the purposes of the class action legislation is not identical to the notion of 'retailer' for the purposes of financial legislation. Hence, for instance, small and medium-sized enterprises, which often qualify as financial 'retailers', cannot benefit from the class action mechanism.

II INTERIM MEASURES

Interim measures that are typically used in banking litigation are summary proceedings (i.e., *inter partes* proceedings that are initiated and handled in an expedited manner in cases of urgency (with the possibility for *ex parte* motions in cases of extreme urgency)); and attachments and similar forms of measures to protect the assets of a debtor against disposal pending the proceedings on the merits.

i Interim measures in situations of financial distress

Interim measures are often requested in summary proceedings by a debtor who is in financial distress or in outright insolvency proceedings (e.g., in US Chapter XI-type restructuring proceedings, where the debtor remains in possession of its business but benefits from a court-supervised payment moratorium and other protection towards its creditors, including its bank creditors).

In such a distress situation, the banks have typically already terminated or accelerated their credit facilities with the debtor because of a lack of fulfilment by the debtor of the terms and conditions of such facilities (e.g., the timely payment of interests or the debtor's compliance with the covenants relating to its financial soundness or with the value of the collateral that the banks have received), or intend to do this during the restructuring. Such termination or acceleration then gives rise to a reimbursement claim of the banks that is immediately due, which the debtor cannot usually meet. In the same scenario, the banks may also start enforcing their collateral or simply refuse to grant any further flexibility to the debtor as regards the use of assets that the debtor has collateralised to the banks. Through summary proceedings, the debtor might try to force the banks to cancel the termination or acceleration of the credit facility and to reinstate the facility, so that the debtor can further

draw on it or, at the very least, is not faced with significant additional outstanding debts. Also, the debtor may try to obtain a court order obliging the banks to refrain from exercising their contractual or statutory security rights (e.g., enforcing a pledge or charge on inventory).

The courts sitting in summary proceedings are reluctant to grant such measures and to interfere in the contractual and statutory rights of the banks towards their debtors. While such courts only assess *prima facie* the rights of the respective parties, and may also carry out a balance-of-interests test (i.e., a test to determine whose interests merit, in view of the legal and factual situation, more protection in the interim pending the resolution of the dispute on the merits), they will typically respect the exercise by a party of that party's contractual or statutory rights (e.g., the termination of a credit facility by a bank for breach of contract by the debtor), unless this exercise constitutes an abuse of rights. Such abuse covers situations in which the beneficiary of a right exercises this right with the sole aim of harming the other party, or without a reasonable and sufficient interest, or in a manner that manifestly exceeds the boundaries of the normal exercise of that right by a normally prudent and careful person (i.e., a bank in this context), or has chosen to act in a way that most harms the debtor.

The same applies to the exercise by bank creditors of their security rights (e.g., the right of a bank that is the beneficiary of a pledge over inventory of its debtor to refuse to give up its control over this pledge by allowing the debtor to use part of this inventory). Belgian restructuring legislation even explicitly sets forth that the prohibition for creditors to take enforcement actions against a debtor that benefits from a court-ordered judicial restructuring, does not affect receivables pledged to creditors. Notwithstanding this provision, courts sitting in summary proceedings have jurisdiction to suspend the enforcement of such collateral rights in situations where the conditions for relief in summary proceedings are met. Courts will, for instance, verify whether, *prima facie*, the banks exercised or relied in a legitimate manner on their security rights. They will, in this context, consider whether the value of the security rights is proportionate to the amount of the outstanding claim. The market value of these rights is, in a distress scenario, typically much lower than the amount of the claim of the banks, in which case there is no issue. By contrast, in the (unlikely) scenario that this value would largely exceed this amount and would not be subject to market fluctuations, the banks could be faced with a court order that mitigates the impact for the debtor of the refusal of the banks to release at least part of the debtor's assets that they hold as collateral. By contrast, courts sitting in summary proceedings have considered, for example, that an immediate enforcement of a pledge was an abuse of right and had to be suspended, as the benefits of such enforcement did not manifestly outweigh the interest of the debtor to ensure the continuity of its undertaking.

ii Anti-suit injunctions

Anti-suit injunctions are one specific form of interim measure on which the Belgian courts occasionally have to rule in cross-border banking disputes. An anti-suit injunction might have the aim of prohibiting one of the parties from initiating proceedings in a jurisdiction other than Belgium, for instance, because the applicant of the injunction considers that its rights of defence will not be sufficiently protected in that foreign jurisdiction.

Belgian courts are also reluctant to grant such injunctions as they consider them to be exceptional and intrusive measures that should only be granted in very limited circumstances where the foreign proceedings that are the subject matter of the injunction would seriously prejudice the rights of the applicant, and be vexatious and oppressive. Common examples of such circumstances are: (1) initiating proceedings in a forum other than the 'natural forum'

for the dispute to give a serious, often tactical, disadvantage to the defendant in that foreign procedure (i.e., the applicant for the injunction) and, thus, to force that party to settle the dispute; or (2) initiating such foreign proceedings in breach of an agreement between the parties to refrain from initiating such proceedings.

III LAWYER–CLIENT PRIVILEGE

i Requirements for recognition of legal privilege

Pursuant to Article 458 of the Belgian Criminal Code, persons entrusted with a duty of confidence by status or by profession (such as attorneys who are members of a bar) cannot reveal confidential information entrusted to them by their clients, except where they are called to give evidence in legal proceedings or where the law requires them to disclose the information in question. This is called professional secrecy. In addition, the Professional Conduct Rules of the Bar forbid a lawyer from testifying to facts that were revealed to him or her during the course of the exercise of his or her profession. However, a lawyer may reveal confidential information if it is necessary for his or her own defence in a criminal or civil case. Case law also indicates that legal professional privilege is enshrined in Articles 6 and 8 of the European Convention on Human Rights.

ii Documents protected by the legal privilege

The documents protected are those that form correspondence between attorneys and their clients, as well as the attorneys' legal opinions and the notes both from attorneys and from their clients regarding these communications. Legal privilege does not apply to the case materials themselves, and official documents, such as judgments or trial briefs, are public. The voluntary communication to third parties of documents protected by professional secrecy will result in those documents no longer being protected.

Correspondence between Belgian lawyers is also confidential in principle and cannot be used as evidence. However, some correspondence between lawyers will be classified as official and can be produced in court. The Professional Conduct Rules of the Bar determine how the distinction should be made. Conflicts are resolved by the head of the bar. Pursuant to Article 5.3 of the Code of Conduct for European Lawyers, correspondence between a Belgian attorney and an attorney from another EU Member State will only be privileged if it is expressly marked as 'confidential' or 'without prejudice'.

Legal actions taken in violation of the attorney–client privilege will be deemed null and void. In civil cases (including in banking disputes), the court cannot accept privileged information as evidence.

iii Recognition of in-house lawyer privilege

In-house counsel are not subject to Article 458 of the Belgian Criminal Code. However, in-house lawyers' privilege has been recognised, to a certain extent, by the Belgian Act of 1 March 2000 establishing a Company Lawyer Institute. Pursuant to Article 5 of this Act, legal opinions rendered by in-house counsel who are members of the Institute, for the benefit of their employers, are confidential.

In-house lawyers' privilege was recognised, with reference to the Act of 1 March 2000, by the Brussels Court of Appeal in a decision of 5 March 2013. While this decision concerned the specific context of an investigation by the Belgian competition authorities, its effect could go beyond this context and strengthen the recognition of this privilege in other areas as well.

Several conditions must be fulfilled before opinions given by in-house counsel may be deemed privileged. The advice must be legal in nature, and not commercial or operational. Only opinions from in-house counsel who are members of the Institute and acting in their capacity as counsel are privileged. The privilege does not extend to mere correspondence. Furthermore, only advice given to the employer (as opposed to third parties) is privileged. The advice will lose its privileged status if it is treated non-confidentially by its author and its addressee. For example, legal opinions circulated to a large number of people may lose their privileged status.

IV JURISDICTION AND CONFLICTS OF LAW

A number of recent banking disputes concerned multiple and complex contractual relations between banks, including Belgian branches of foreign banks, and their clients, particularly large corporates that have a cross-border customer base. These relations may, for instance, consist of a credit facility granted by the bank as well as a derivatives transaction entered into by the client with the same bank, typically to hedge its foreign exchange or interest rate exposure.

In such cases, the credit facility is often governed by Belgian law with the jurisdiction of the Belgian courts in case of disputes, while claims under the derivatives transactions are to be settled by an English-governed International Swaps and Derivatives Association agreement, for example, with the exclusive jurisdiction of the English courts. Belgian courts typically enforce such clauses rigorously. Thus, they will refuse to handle proceedings brought by the client against the bank with claims under both the credit facility and derivatives, and will instead raise their lack of international jurisdiction for the derivatives claims.

V SOURCES OF LITIGATION

There are various sources of banking disputes in Belgium.

First, there is the traditional banking litigation regarding credit facilities and related disputes between a bank and its borrowers. This litigation might also include liability claims by a debtor – or its trustee in case the debtor has been declared bankrupt – against the lender for having unduly granted, maintained or terminated a credit facility.

Since the 2008 financial crisis, there has also been a growing number of disputes involving banks that concern derivatives transactions or similar financial products, as well as disputes between banks and clients (typically corporates or wealthy individuals) to whom the banks offered advisory (or discretionary) portfolio services, and who are unhappy about the performance of their portfolio (i.e., mis-selling claims).

Large-scale mis-selling claims typically involve allegations that misleading or insufficient information was provided prior to the transaction being entered into. However, it is not only contract and financial law that are relevant in such disputes – an issue that increasingly arises is the tension between financial and consumer protection legislation. Retail investors (who, as aforementioned, are not included in the definition of ‘consumers’ under Belgian law), in particular, argue that even if a financial institution has complied with all the information obligations that are contained in financial legislation (e.g., under MiFID or the Prospectus Law), it may still be liable under consumer protection legislation for having misrepresented the information provided to them. In certain areas, such as the public offer of financial instruments, the legislator has adopted statutory rules that exclude such argument. Such

rules unfortunately do not exist in every area where financial law requirements might conflict with consumer protection considerations. In addition, while Belgian mis-selling legislation is driven by EU law, it often goes beyond a mere one-to-one implementation of the EU law requirements. Investor-friendly rules are often added, for instance, to remove the evidentiary burden from claimants (see Section I, above).

Even outside the ambit of class actions, mis-selling disputes can easily be initiated by groups of investors that act collectively, usually on the basis of background initiatives by investor advocacy organisations who offer to represent their interests on a for-pay basis.

In Belgium, mis-selling and related financial disputes typically consist of a mixture of large-scale civil litigation, criminal proceedings and regulatory investigations, which are pursued in parallel. Legal entities can be criminally prosecuted in Belgium, and financial institutions can be criminally prosecuted for banking practices, either with or without their directors or senior managers. In Belgium, settlements of mis-selling claims with the regulatory and criminal authorities, for example, are possible but must be separately negotiated and entered into. They typically require that the financial institution concerned satisfactorily indemnifies the investors.

In the past, the Belgian criminal authorities were traditionally more active than the financial regulators in enforcing and sanctioning practices that affected retail investors. However, the significant enforcement and sanctioning powers that regulators have obtained, together with the changed regulatory and policy environment following the 2008 financial crisis, have led to an increased activism by regulators to challenge certain banking practices, especially in relation to retail investors. This trend is expected to continue.

Finally, a specific source of banking litigation is appeals by financial institutions against regulatory decisions of Belgian financial supervisors, such as the National Bank of Belgium as banking supervisor, and the Financial Services and Markets Authority as markets supervisor. The Brussels Court of Appeal has exclusive jurisdiction for such appeals. Since the establishment of the single supervisory mechanism (SSM) and the single resolution mechanism (SRM), eurozone banks are also subject to the supervision and rules of the SSM and SRM. The respective key regulators (i.e., the Frankfurt-based European Central Bank for the SSM and the Brussels-based Single Resolution Board for the SRM) have far-reaching supervisory powers that may directly affect individual banks. Disputes in this area can be brought, and have effectively already been brought, before the European courts in Luxembourg.

VI EXCLUSION OF LIABILITY

The 2008 financial crisis led to a number of mis-selling claims in Belgium, including by corporates and institutional investors. Before the transposition of MiFID in Belgian law, the generally accepted view was that financial institutions had considerable contractual freedom to limit their liability for mis-selling claims by institutional investors, including for gross negligence. The only limitation was the financial institution's own fraudulent or wilful misconduct. Under the MiFID I rules, as transposed in Belgium, banks may not exclude their common law liability in contracts with non-professional clients regarding portfolio management services.³ A few legal scholars have raised the question of whether this prohibition should be extended to certain other contracts entered into by financial institutions, including

³ See Article 20, Section 4 of the Belgian Royal Decree of 3 June 2007 setting forth specific rules for the implementation of the directive concerning markets in financial instruments.

with institutional investors. This view seems questionable, as the contractual freedom to limit or exonerate contractual and tort liability in the context of a sale of financial instruments by financial institutions to institutional clients still exists, subject to the traditional exception of fraudulent or wilful misconduct.

VII REGULATORY IMPACT

As mentioned in Section I, above, banking litigation is significantly impacted by regulatory legislation, most notably the current MiFID I rules and their transposition in the respective national laws of the Member States, such as in the Law of 2 August 2002 in Belgium.

While MiFID I aims to lay down harmonised rules for the protection of investors throughout the European Union, it does not harmonise the civil consequences for the investors concerned in case of a breach of one of these rules by the bank. The Court of Justice of the European Union (CJEU) confirmed this on 30 May 2013 in the *Genil/Bankinter* case. The CJEU nonetheless referred to two principles that relate to the civil consequences of MiFID I breaches that EU Member States need to apply when transposing MiFID I. First, the principle of effectiveness requires that Member States ensure that mechanisms are in place for the payment of compensation or other remedial action in case of financial loss or damage suffered as a result of an infringement of the rules. MiFID II (see below) now explicitly codifies this principle (see Article 69(2), last paragraph of the MiFID II Directive). Second, the principle of equivalence requires that Member States must, for breaches of EU law (e.g., the MiFID rules), provide for the same remedies and procedural mechanisms to affected persons as those that exist for breaches under purely domestic law.

The MiFID I legislation has been substantially amended and upgraded by the MiFID II legislation. Contrary to MiFID I, which consists of an EU Directive, MiFID II consists of two different legal instruments: a Directive,⁴ which requires transposition in the respective national laws of the EU Member States, and a Regulation,⁵ which contains directly applicable rules for the trade and regulatory transparency requirements applicable to investment firms, regulated markets and data reporting services providers, which will uniformly apply throughout the EU without the need for further transposition in domestic law.

MiFID II increases the level of protection for professional clients by bringing them under the umbrella of certain information obligations that are currently already applicable to retail clients under MiFID I. MiFID II also imposes new disclosure obligations in relation to the execution policy of a bank. The bank will have to explain in a clear, detailed and understandable manner how orders are executed. The requirement for prior express consent from the client for certain transactions will also be broadened. These requirements might, in case of problems with transactions, trigger claims by clients that they did not give proper consent and that the transactions should therefore be declared null and void because of a lack of consent. Another area that is often a bone of contention in banking litigation regarding investment services concerns the level of knowledge and experience of a client in relation to

4 Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61 (OJ L 173, 12 June 2014, p. 349).

5 Regulation (EU) No. 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No. 648/2012 OJ L 173, 12 June 2014, p. 84.

the financial instruments that are the subject matter of the transaction (i.e., issues revolving around ‘appropriateness’ and ‘suitability’). MiFID II will also increase the banks’ duties in this area.

EU Member States, including Belgium, must transpose the MiFID II Directive into their respective legislation so that it may be applicable as of 3 January 2018 (the original deadline given in Article 93(1), second paragraph of the MiFID II Directive was 3 January 2017). Draft legislation to this effect is currently under discussion in Parliament.

BRAZIL

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I OVERVIEW

Brazil is a highly litigious country. The number of civil lawsuits related to financial and banking litigation is significant and involves all financial institutions, such as banks, payment agencies, credit card companies, banking correspondents, investment funds and insurance companies.

Banking litigation typically arises from contractual default or disputes on financial transactions, interest rates, loans, improper charges, pricing and products, or services defects. The principal matters related to banking litigation currently under discussion before Brazilian courts are discussed below.

i Monetary stabilisation plans

From 1986 to 1994, the Brazilian federal government implemented several consecutive monetary stabilisation plans (MSPs), to combat hyperinflation. In order to implement these plans, the federal government enacted several laws based on its power to regulate the monetary and financial systems as granted by the Brazilian Federal Constitution (the Constitution).

Holders of savings accounts during the periods when the MSPs were enacted have challenged the constitutionality of the laws that implemented those plans, claiming additional amounts of interest from the banks where they held their savings accounts based on the inflation rates applied to savings accounts under the MSPs. As a result, Brazilian financial institutions became defendants in numerous standardised lawsuits filed by individuals, consumer protection associations or public attorneys' offices in respect of the MSPs. Holders of savings accounts may collect any amount owing on account of a final decision.

The Federal Supreme Court (STF) has issued a number of decisions in favour of such holders, but has not issued a final ruling with respect to the constitutionality of the MSPs as applicable to savings accounts. In relation to a similar dispute with respect to the constitutionality of the MSPs as applicable to time deposits and other private agreements, the STF has decided that the laws were in accordance with the Constitution. In response to this discrepancy, the National Confederation of the Financial System, an association of Brazilian financial institutions, filed a special proceeding before the STF,² arguing that holders of savings accounts did not incur actual damages and that the MSPs as applicable to savings accounts were in accordance with the Constitution.

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2 ADPF No. 165.

Currently, the matter is pending a final decision. All actions on the subject without a final judgment have been suspended since the STF recognised the general repercussion of the disputes and decided to judge four appeals assigned as ‘leading cases’.³ This means that what is decided with regard to these appeals will be valid for all similar lawsuits, presently suspended.

At the end of 2017, consumer protection associations – including the Brazilian Consumer Defence Institute (IDEC), the Brazilian Association of Consumers’ Rights and the Brazilian Savers’ Institution – jointly with the Brazilian Bank Federation and the National Financial System Confederation, reached a collective settlement agreement with the purpose of solving disputes related to MSPs.

The settlement agreement, which was mediated by the Federal Attorney General, provides for the payment, by the financial institutions, of the amounts corresponding to the inflationary purges of savings on behalf of consumers, according to the limits and criteria set forth in the instrument.

In March 2018, the STF’s plenary session ratified the collective agreement within the appeals assigned as ‘leading cases’, to produce legal effects based on Article 487(III)(b) of the Code of Civil Procedure.⁴ According to the STF, the agreement will close collective actions related to the matter, as well as solve thousands of individual lawsuits filed by consumers who choose to adhere to its terms.

The STF also determined the stay of the appeals for a period of 24 months, so that consumers that meet the criteria established under the agreement may voluntarily adhere to its terms, by means of an electronic platform.⁵ Hence, consumers’ adherence to the agreement is not mandatory. In the case a consumer opts-in, the Court will dismiss the individual lawsuit with prejudice.

If, however, a consumer chooses not to adhere to the agreement within the 24-month period, it will no longer be possible to do so. In this case, the individual lawsuit will continue in its normal course.

Note that the STF expressly established that the ratification of the collective agreement signed by consumer protection associations and financial institutions does not imply any commitment of the STF to the juridical thesis contained in the appeals affected as leading cases. This means that the STF has not decided on the merits of the matters under discussion.

II LEGISLATION

i Regulatory

In 2001, in order to improve the relationship between market participants and foster additional transparency, discipline, competition and reliability on the part of financial institutions, the National Monetary Council (CMN) established and consolidated a new set of procedures regarding the settlement of financial transactions and services provided by financial institutions to customers and the public in general.

These rules have been revised and are now consolidated in Resolution 3,694 of 26 March 2009, which were substantially amended in 2013 and again in 2016. The aim of the regulations is to prevent risks of litigation in the contracting of transactions and rendering

3 Extraordinary appeals Nos. 626.307, 591.797, 631.363 and 632.212.

4 ‘Adjudication on the merits will occur when the judge: III. certifies: (...) (b) a settlement.’

5 www.pagamentodapoupanca.com.br.

of services to clients. The CMN and the Central Bank have also been issuing regulations with respect to operational risk, in order to have stricter control and avoid litigation risks, following Basel Accord guidelines.

In Resolution 3,694, financial institutions must ensure that in their transactions and services to customers:

- a* the products and services being offered or recommended are adequate for the needs, interests and objectives of clients and users (suitability);
- b* the transactions are carried out in a comprehensive, reliable, safe and confidential manner, and the transactions and services rendered are legitimate;
- c* the necessary information to allow for the client's and user's free choice and decision-making processes, including rights, duties, responsibilities, costs or advantages, penalties and possible risks when carrying out a transaction or rendering a service, is timely provided;
- d* the client or user is timely provided with agreements, receipts, statements, advice and other documents related to the transactions and services, as well as the possibility of timely cancellation of the agreements;
- e* clear, objective and adequate wording is being used, in relation to the type and complexity of the transaction or service involved, in contracts, receipts, statements, vouchers and other documents intended for the public, thus allowing for a clear understanding of the content and terms, values, charges, fines, dates, places and other conditions involved;
- f* an adequate instrument has been put in place to set out the rights and obligations concerning the opening, use and maintenance of a post-paid payment account;
- g* to forward a payment instrument to the client's or user's residence or to enable the respective instrument only upon express request or authorisation; and
- h* identification of final users' beneficiaries of payments or transfer in statements and bills of the payer, including in situations in which the payment service involves institutions participating in different payment arrangements.

With regard to point (c) above, when a deposit account or payment account is opened, it must be accompanied by a booklet containing essential information and it must, at minimum, explain the basic rules, existing risks, contracting and termination procedures, safety measures (including in case of loss, theft or hacking of credentials), and the method and timing for updating of record data by clients.

Financial institutions must disclose, on their own premises and at the establishments where their products are offered, in a visible place and in legible form, adequate information on the circumstances that give rise to refusal of payments or acceptance of checks, payment slips, documents (including collection documents), bills, etc.

Financial institutions are prohibited from refusing or impairing access to ordinary customer service channels (including cashiers) by clients and users of their products and services, even when such institutions offer alternative or electronic customer service mechanisms. These provisions do not apply to virtual establishments or to the provision of collection and receipt services arising from contracts or agreements that provide for specific customer service channels.

The option for providing services through alternative means is permitted, provided that the necessary measures have been taken to safeguard the integrity, reliability, security, safety

and confidentiality of transactions carried out, as well as the legitimacy of services provided, with regard to the rights of clients and users, who shall be informed by the institutions about the existing risks.

All of these rules are set forth in a generic nature, and there is no specific guidance on their implementation, except for the day-to-day contact between the financial institutions and the Central Bank as the supervising entity.

In the event such regulations are not observed, financial institutions are subject to administrative penalties issued by the Central Bank, in addition to liabilities in the civil sphere already discussed.

ii E-payments Law

Over the past decade, the volume of transactions using payment instruments in the wholesale market increased significantly. In view of this, in 2013, the federal government enacted the E-payments Law,⁶ which provides the legal framework for 'payment arrangements' (i.e., the set of rules governing a payment scheme, such as credit or debit card transactions), and 'payment agents' (i.e., any agent that issues a payment instrument or acquires a merchant for payment acceptance), which became part of the Brazilian Payment System and subject to oversight by the Brazilian Central Bank (the Central Bank). It is noted that payment agents are not deemed to be financial institutions and are prohibited from engaging in activities that are exclusive to these institutions.

The E-payments Law brought within the scope of the CMN and the Central Bank supervision the entire market of credit, debit and prepaid cards that were not previously regulated.

Following the E-payments Law, the CMN and the Central Bank enacted a set of rules on payment arrangements and payment agents, which became effective in May 2014. This set of rules encompasses, among others: (1) consumer protection and anti-money laundering compliance and loss prevention rules that should be followed by payment agents and payment arrangers; (2) the procedures for incorporation, organisation, authorisation and operation of payment agents, as well as for the transfer of control, subject to the Central Bank's prior approval; (3) payment accounts, which are broken down into prepaid and post-paid accounts; and (4) a liquidity requirement for prepaid accounts by which their balance must be allocated to a special account at the Central Bank or else invested in government bonds, starting at a lower rate and rising gradually to the total account balance.

Following discussions with market players and industry representatives, the Central Bank has been adjusting and improving the regulations over time, mainly to include operational and non-discriminatory tools to foster competition in the payments market.

III PROCEDURAL ISSUES

In Brazil, banking litigation is not subject to a specific law. Disputes involving banks and other financial institutions are governed by the provisions of the Code of Civil Procedure.

On 18 March 2016, the New Code of Civil Procedure⁷ (the New Code) came into effect, which brought changes to the procedure rules in force since 1973.⁸ The New Code

6 Law 12.865 of 9 October 2013.

7 Federal Law No. 13,105 of 16 March 2015.

8 Federal Law No. 5,869 of 11 January 1973.

aims to simplify the procedural action, as well as to favour the celerity of disputes and effectiveness of the result of the proceeding. The New Code also has as one of its main purposes the granting of greater autonomy to the parties to manage how to pursue the lawsuit (i.e., setting deadlines, hearings, acceptable evidence).

The main changes brought about by the New Code are outlined below.

i Promoting mediation

Considering that litigation is common in Brazil, and in view of the increasing number of lawsuits filed before national courts, the New Code strives for stimulation of settlements, by strengthening mechanisms such as mediation and conciliation, in order to decrease the number of claims.

In this scenario, the New Code makes mandatory a conciliation or mediation hearing at the beginning of the proceeding, even before the defendant presents his or her answer to the complaint. There may be as many sessions designed for conciliation and mediation as necessary for the parties to settle, during a period not exceeding two months from the date when the first session is held (Article 334).

ii Procedural transaction

The New Code sets forth crucial measures to give autonomy to the parties to decide on their dispute. If the suit deals with rights that are open to settlement, parties may lawfully provide for changes in the proceeding to adapt it to the specificities of the case and to stipulate procedural obligations, powers, privileges and duties, before or in the course of the proceeding (Article 190).

Contenters set such changes through ‘procedural transaction’, which may consider, among other matters, the burden of proof, production of evidence, forum selection, waiver of the right to appeal, deadlines and arbitration agreement.

iii Standardising judicial precedents

The New Code requires that higher courts (i.e., state courts and regional federal courts) standardise their precedents and keep them stable, fair and consistent, and issue guiding precedents based on their prevailing court rulings (Article 926).

It also provides that, when judging disputes, judges and courts shall observe (1) the STF’s decisions rendered under the model of centralised constitutional review; (2) binding precedents; (3) appellate decisions rendered in incidental proceedings for assumption of jurisdiction or for resolution of same subject-matter suits, and in the judgment on extraordinary and special appeals on the same matter of law; (4) guiding precedents set by the STF and the Superior Court of Justice (STJ); and (5) the stand of the full bench or special body to which they report (Article 927).

iv Resolution of repetitive lawsuits

Brazil has an excessive number of lawsuits in progress before national courts, many of which have similar legal issues under discussion. In view of this, the New Code shaped a measure named ‘incident for resolution of repetitive demands’ that enables appellate courts to simultaneously solve different cases that contain controversy regarding the same legal matter, provided that there is a risk of harm to equality and legal certainty (Article 976).

When a certain legal issue is highly recurrent, the judge, the parties or the Public Prosecutor's Office may request an incident for resolution of repetitive demands to the court's president. Once the incident is assigned, the reporting justice orders suspension of all pending individual lawsuits or class actions on the same matter, in the state or region.

After the incident is ruled, the decision shall be applied to (1) all individual or class actions dealing with an identical matter of law and being processed in the jurisdiction of the respective court; and (2) future cases that deal with an identical matter of law and are processed within the territorial jurisdiction of the court.

With regard to banking litigation, currently, there is one main incident pending judgment, regarding the level of abuse of interest rates involving bank contracts.⁹

v Interim measures

Interim measures are granted by the court to provide urgent relief, in order to avoid any harm to the effectiveness of the process or damages that may result from its delay.

The Code of Civil Procedure 1973, repealed in March 2016 by the New Code, used to provide for different types of provisional measures, referred to as 'typical provisional measures' (i.e., anticipated discovery motion, precautionary measure for disclosure of documents, seizure precautionary measure), to prevent, preserve or defend the parties' rights before the conclusion of the lawsuit.

The New Code simplified the legal system previously in force, henceforth stipulating that the party may request a provisional relief based on urgency or evidence (Article 294), entered before the lawsuit is filed or incidentally.

The court will grant a relief based on urgency when there are elements evidencing the likelihood of an asserted right and a risk of injury or risk to the practical result of the proceeding. The court may enforce this relief through seizure, sequestration, inventory of assets, registration of protest against disposal of assets, and any other valid measure to assure the asserted right.

When the condition of urgency is concurrent with filing of the suit, the complaint may be limited to a request for advance relief, specifying the claim for final relief and detailing the dispute, the right sought, and the risk of damage or the risk to the ultimate outcome of the case. Should the court grant the relief, the opposing party must file an interlocutory appeal against the relevant decision (Article 303). If the defendant fails to appeal, the advance relief becomes permanent, causing the dismissal of the case.

In addition, the interested party may plead relief based on evidence, regardless of proof of any risk of damage or risk to the case's practical result, when, among other cases, the defendant is manifestly abusing its right of defence or making use of delaying tactics; or the statements of fact may be evidenced only by documents, and a legal principle has been settled in a judgment on same subject-matter suits or in a binding precedent (Article 311).

Furthermore, although the New Code has extinguished the typical provisional measures set forth by the previous Code, it expressly authorises judges to apply any measures that they consider appropriate to enforce provisional relief (i.e., seizure, sequestration and inventory of assets), regardless of the parties' request, including in collection actions, which frequently involve financial institutions.

9 Lawsuit No. 0872123-67.2016.8.13.0000 – Minas Gerais State Higher Court.

In respect to collective actions, legal doctrine recognises that judges may also apply measures of psychological pressure on the defendant or debtor to guarantee compliance with financial obligations (e.g., suspension of driver's licence, restriction of passport, cancellation of the debtor's credit card), even though these measures do not ensure the immediate satisfaction of the debt.

IV PRIVILEGE AND DISCLOSURE

The Constitution provides protection to lawyers in the exercise of their profession. Such protection is reflected in the Lawyers and Brazilian Bar Association's Statute,¹⁰ which guarantees the inviolability of lawyers' offices or place of work, as well as of their working instruments; and written, telephonic and telematic mail, as long as they are related to the performance of the profession.

Regarding professional secrecy, the Ethics Code of the Brazilian Bar Association¹¹ sets forth that lawyers have the duty to keep confidential all facts of which they become aware as a result of the profession. Communication of any nature between lawyers and their clients is presumed to be confidential.

Lawyers are also not obliged to testify, in judicial or administrative proceedings, on matters to which they must maintain professional secrecy. Moreover, when applying on behalf of third parties, against ex-client or former employers, lawyers must safeguard professional secrecy.

Professional secrecy is a public policy principle. Thus, it is not dependent on the client's confidentiality request. Notwithstanding, professional secrecy might be disregarded in exceptional circumstances for justified reasons, such as in cases of serious threat to the right to life and honour, or in situations of self-defence. In addition, Brazilian courts recognise that professional secrecy might be disregarded in cases where the lawyer is suspected of unlawful behaviour (i.e., the lawyer becomes an accessory to the crime that is being investigated).

V JURISDICTIONAL MATTERS

Brazilian courts have exclusive jurisdiction to decide on actions relating to real property located in Brazil; to examine and decide on probate proceedings of a deceased person's Brazilian estate, even in cases where the deceased was a foreigner and resided abroad; and in divorce, judicial separation or dissolution of cohabitation, to provide for distribution of property located in Brazil, even if the owner is a foreigner or is domiciled abroad.

In addition, the filing of a lawsuit before a foreign court does not prevent Brazilian courts from ruling the same case if: the defendant, regardless of his or her nationality, is domiciled in Brazil; the obligation is to be performed in Brazil; or the actions result from an event that occurred or an act performed in Brazil.

Brazilian courts have jurisdiction to adjudicate lawsuits arising from consumer relations, when the consumer is resident or domiciled in Brazil. Accordingly, Brazilian courts shall have concurrent jurisdiction to rule claims involving clients of financial institutions resident or domiciled in Brazil even if a lawsuit is filed abroad.

10 Law No. 8,906 of 4 July 1994.

11 Resolution No. 02/2015.

Article 25 of the New Code provides that Brazilian courts have no jurisdiction to process and adjudicate on a lawsuit when there is a clause electing an exclusive foreign forum in an international contract. Nevertheless, such provision does not apply to the principle of exclusive jurisdiction, mentioned above.

To that extent, financial contracts might provide for a contractual clause selecting the jurisdiction to which eventual disputes between the contracting parties will be submitted, regardless of any specific connecting factor to Brazil. Nonetheless, courts may render the forum selection clause ineffective, especially in cases involving consumers.

This is because consumer relations in Brazil are ruled by the Consumer Protection Code,¹² a law issued to protect the consumers. Section 101(I) of the Code provides that consumer disputes will be processed and judged in the jurisdiction of the consumer's domicile.

Nevertheless, the rules of the Consumer Protection Code apply only to agreements entered into between suppliers and users to supply products or services. Brazilian law does not present a clear concept of 'end user', however.

Currently, there are two different schools of thought regarding the concept of 'end user'. The first, known as the maximalist school, advocates that 'end user' refers to a practical perspective, meaning that if an entity or person acquires a product or service and is not going to resell such product or service to a third party, it should be considered the end user of such product or service, for legal purposes.

That is to say that, even if the person or entity acquires the product or service as supplies entering into its manufacturing process, it should be considered the end user of the supplies. Thus, the Consumer Protection Code would rule the relation existing between such end user and the supplier of the goods or service.

The second school of thought, the finalist school, understands that the concept of 'end user' has an economic nature. To that extent, if the person or entity acquires supplies that will be used in its manufacturing process, it should not be considered the end user of the supplies. This concept should also be considered to have a commercial nature as it is ruled by the Civil Code. This is the standing adopted by most Brazilian scholars.

After a number of conflicting decisions on the matter, the STJ reached the conclusion that the individual that acquires goods or services to be used in its manufacturing chain in a for-profit activity, is not a consumer in the legal sense of the word (finalist school). Notwithstanding this, the STJ allows exceptions to this rule in cases where the end user is vulnerable compared with the supplier, allowing the application of the Consumer Protection Code.

Specifically concerning financial products and services, after extensive debates, Brazilian courts held that they are subject to the Consumer Protection Code,¹³ as long as the counterparty to the agreement is regarded as an end user, that is, a person acquiring the products and services but not using them for profit-making purposes.

Consequently, Brazilian courts may deem a forum selection clause invalid when provided under a financial contract involving a consumer (end user). In this case, the dispute will be processed and ruled in the jurisdiction of the consumer's domicile, pursuant to the Consumer Protection Code.

12 Law No. 8,078 of 11 September 1990.

13 Precedent 297. The Consumer Protection Code is applicable to financial institutions.

In any event, if the financial contract does not involve a consumer, the financial institution and the counterparty may elect a foreign court to settle any disputes that may arise from such contract, in accordance with Article 25 of the New Code.

VI FREQUENT CAUSES OF ACTION

There is a substantial number of lawsuits involving financial institutions in Brazil.

Lawsuits engaging financial institutions as plaintiffs most commonly concern credit collections arising from clients' default. On the other hand, disputes engaging financial institutions as defendants are usually related to consumer matters, such as lawfulness of MSPs; improper registration of consumers in credit protection agencies; and irregularities related to the integrity, reliability, security, secrecy or legitimacy of operations and services offered to clients.

There are also several lawsuits filed by consumers against financial institutions claiming the reduction of interest rates set forth in financial contracts. Such lawsuits derive from the fact that, in Brazil, there is no legal provision limiting interest rates in banking transactions. Thus, the contracting parties are free to negotiate interest rates that are convenient.

Based on the Consumer Protection Code, however, courts may review the agreements already signed and determine a reduction in the agreed-upon interest rate if it holds that said interest rate causes unreasonable disadvantage for the consumer. On this subject, the STJ also stated that it may review a banking agreement entered into by a consumer if the financial institution charges blatantly excessive interest rates.

Within this context, financial institutions face mass litigation because of consumer claims, pleading the reduction of charged interest rates in defaulted agreements. Nevertheless, as a rule, only when the agreed-upon interest rate is higher than the average market rate should the contractual revision occur.

VII LIABILITY

Brazil's civil liability system is based on the general provisions of the Civil Code. According to this system, a person will be held civilly liable in case it carries out an illicit act and there is causation between such illicit act and the loss caused to the aggrieved party.

In principle, there is no separate legal framework for financial institutions when it comes to civil liability. Nevertheless, as mentioned above, the STJ has already decided that the Consumer Protection Code, which provides for specific rules on suppliers' liability, is applicable to the relationship between financial institutions and consumers.

Therefore, as outlined in subsections i and ii, below, Brazil has a dual system of liability for financial institutions: (1) for corporate clients, the basic principles of civil law liability established in the Civil Code; and (2) for consumers, a more protective system based on the Consumer Protection Code.

i The Civil Code

The general rule of civil liability under Brazilian law arises from Sections 186 and 927 of the Civil Code, by which a person is liable to redress the damage caused to another person resulting from its fault or wilful misconduct.

Brazilian law divides civil liability into at-fault liability and strict liability. Sections 186 and 927 (main section) of the Civil Code set forth the general rule of at-fault liability. According to the doctrine, in order to characterise at-fault liability, the agent must carry out an illicit act, for the purposes provided in Section 186.¹⁴

Section 927, sole paragraph, of the Civil Code sets forth the general rule of strict liability. According to this provision, an agent may be held liable independent of fault when such agent is subject to strict liability, regardless of whether there has been an error in conduct.

Strict liability is, therefore, liability grounded on risk, which consists of:

*the obligation to compensate for the damage caused as a result of activity developed concerning the agent's interest and under its control, without any questioning on the behaviour of the aggrieved party, setting such liability as strict, that is to say, in the relationship of cause and effect between the damage itself and the conduct taken by the party causing such damage.*¹⁵

Hence, at-fault liability differs from strict liability to the extent that at-fault liability requires the existence of fault in the conduct of the agent, while strict liability depends only on the existence of a causal relationship between the conduct and the damage.

Most of the relationships between financial institutions and their clients are subject to at-fault liability. That is to say that the client has the burden of proof to show the illicit act (fault), the damage and the causation between both.

Nonetheless, court precedents have shown situations in which there is strict liability of financial institutions, based on the understanding that a financial institution's activities can cause risk to the rights of other parties, as provided under the sole paragraph of Section 927 of the Civil Code.

Based on this rule, the STJ has issued interpretative rulings to standardise the interpretation of courts to some specific situations of strict liability (i.e., financial institutions are strictly liable for damage caused by *force majeure* events that are the result of fraud and misdemeanour activities carried out by third parties in banking transactions).¹⁶

There is no legal provision in the Civil Code that forbids financial institutions to include contractual clauses that provides for the exclusion of liability if (1) the financial institution does not act with grave fault or wilful misconduct; and (2) the other contracting party is not considered a consumer under Brazilian law, as detailed in subsection ii, below.

ii The Consumer Protection Code

Generally, the Consumer Protection Code assumes that the consumer is always the weakest party in the relationship between supplier and consumer. Within this context, application of the Consumer Protection Code will be, as a rule, more favourable to the victim because it not only imposes strict liability on the offender, but also encompasses a whole set of rules that favour the consumer.

14 As per Section 186 of the Civil Code, anyone who, by voluntary act or omission, negligence or recklessness, violates law and causes damages to others, including non-pecuniary damages (i.e., moral damages), commits an illicit act.

15 Maria Helena Diniz. *Curso de Direito Civil Brasileiro: Responsabilidade Civil*, seventh volume. São Paulo: Saraiva, 2002, p. 49.

16 Interpretative ruling No. 479 of STJ.

A special chapter in the Consumer Protection Code is devoted to consumer protection under contracts. A section of this chapter focuses on abusive clauses, which are considered null and void by operation of law. This section deems invalid any contractual clause that prevents, disclaims or reduces the supplier's liability for defects of any kind in the products and services, or entails a waiver or disposal of right.

The Consumer Protection Code also provides that parties may limit the amount of indemnification suppliers may pay to consumers in case of consumer agreements entered into with corporations (i.e., non-individual consumers), in justifiable situations. Although the law does not provide for a concept of 'justifiable situation', legal doctrine holds that it may be reasonable to limit indemnification in case there is a clear upside to the consumer as a trade-off to such limitation (i.e., the price paid for the product or service is reduced owing to such limitation).

iii Liability regime applicable in banking litigation

Given the above-mentioned considerations, financial institutions' liability regimes may vary depending on the nature of the relationship maintained with the counterparty.

When it comes to consumer relations, financial institutions are strictly liable for damages caused to consumers, based on the provisions of the Consumer Protection Code. In these cases, contractual provisions or terms of business restricting financial institutions' liability shall be considered null and void by Brazilian courts. As described above, however, in a relationship between the supplier and a corporate consumer, civil liability may be limited in justifiable situations.

Conversely, there being no consumer relation between the contracting parties, the case will be governed by the Civil Code, which does not prohibit the insertion of clauses that exclude or limit financial institutions' liability, provided that it does not limit financial institutions' liability in case of grave fault or wilful misconduct.

VIII OUTLOOK AND CONCLUSIONS

The New Code changed the procedural rules previously in force, to favour the efficiency of disputes and effectiveness of the result of judicial proceedings. Among other changes, the New Code strengthens alternative methods of conflict resolution, such as mediation and conciliation, aiming to reduce the number of claims.

Considering the new legal system introduced by the New Code, and the high rate of recurrence of judicial complaints involving financial products and services, financial institutions, along with the courts, are likely to take internal measures to promote the amicable resolution of conflicts and celerity of disputes.

Examples of such measures are the creation of conciliation centres to promote conciliation exclusively in banking disputes – as established by the São Paulo State Higher Court in 2016 – and fostering administrative actions within financial institutions to internally solve consumer complaints and avoid judicial disputes.

In addition, the above-mentioned ratification, by the STF, of the collective agreement regarding MSPs entered into by consumer protection associations and financial institutions shows that courts are promoting and prioritising the consensual solution of conflicts, in accordance with the guidelines of the New Code.

As stated, the execution and ratification of the collective settlement agreement will resolve thousands of lawsuits involving the matter, and bring better balance and stability to the National Financial System.

Finally, the CMN and the Central Bank have been acting on a preventive basis, through regulations that aim to avoid conflicts with clients and reduce operational risks facing Brazilian financial institutions. Despite all of this, Brazil continues to have a highly litigious banking system, so all these efforts must continue to increase customer satisfaction and reduce the level of litigation.

CANADA

Graeme A Hamilton, Mathieu Lévesque and D Ross McGowan¹

I LEGISLATION AND JURISDICTION

i Legal and regulatory patchwork for financial services across Canada

The Canadian legal system is characterised by the coexistence of both civil and common law provinces within a federal parliamentary system. Civil law is exclusively applicable in the province of Quebec, whereas common law applies in Canada's other nine provinces and three territories. The civil law tradition in Canada finds its origins in France. The common law tradition originates from British colonisation of what is now the rest of Canada.

Under the Canadian Constitution, each provincial legislature has general jurisdiction over property and 'civil law' (meaning commercial law and commercial transactions), while the federal parliament has an exclusive or paramount jurisdiction over certain private law matters, including banking, issuance of currency, bills of exchange and bankruptcy and insolvency. The country's legal system leaves open a concurrent jurisdiction between provincial and federal powers over certain legal matters. This leads to a challenging regulatory compliance landscape for those entering or operating in Canada's financial services industry. Examples of these challenges include compliance issues with an array of provincial consumer protection laws, various federal and provincial privacy laws, differential laws for issuing securities, provincially unique requirements for loan and mortgage security and a broad array of other areas of overlapping jurisdiction. There is a particular interdependence between federal and provincial legislation. This tends to cause significant challenges in terms of regulatory compliance for businesses needing to harmonise their legal compliance for operations across Canada.

The federal parliament legislates federal laws that seek to reconcile the coexistence of two fundamentally different legal systems, all within a bilingual (English and French) context. Federal statutes generally operate throughout Canada, such as the Criminal Code, the Competition Act and the Bills of Exchange Act. Further, certain commercial statutes, such as the Bank Act and the Trust and Loan Companies Act create the framework to regulate Canada's federally incorporated financial institutions.

At the provincial level, financial services businesses and financial institutions may be incorporated under applicable provincial laws for money services businesses, certain savings and loan institutions, payment processing and other related endeavours. Generally, provinces have legislative and regulatory authority limited to those entities incorporated

¹ Graeme A Hamilton, Mathieu Lévesque and D Ross McGowan are partners at Borden Ladner Gervais LLP (BLG). The authors hereby wish to thank Frédérique Drainville, associate, for her precious contribution in the preparation of this article.

or doing business within the provincial boundaries. Provincially incorporated entities that operate across provincial boundaries may thus be subject to the jurisdiction of multiple regulatory authorities.

The main purpose of the Bank Act and its related statutes and regulations is to provide a legislative framework that promotes the efficiency and security of the financial system in Canada, and to set national standards applicable to banking products and services. The federal authorities further regulate the 'business of banking' and related services directly or indirectly through regulators and rule makers such as the Office of the Superintendent of Financial Services (OSFI); the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC); the Financial Consumer Agency of Canada (FCAC); Canada Mortgage and Housing Corporation (CMHC); and the Canada Deposit Insurance Company, as well as other entities within federal jurisdiction.

While some of the regulatory agencies have express authority to make and impose rules on entities operating in the area of financial services (OSFI and FINTRAC), others, such as the FCAC, have a hybrid regulatory power, applied in part by way of rights to investigate, enforce and fine for non-compliance, and in part by way of creation of 'voluntary' compliance codes that have been adopted by the Canadian financial services industry as business standard operating protocols, ignored at their peril. Regulation of the financial services industry in Canada is also accomplished by rules created by statutory corporations. One example is CMHC, for mortgage rules applicable to requirements for qualifying for mortgage insurance and securitisation of mortgage pools. Similarly, the Canadian Payments Association (now known as Payments Canada) sets the automated clearing and settlement system rules and large value transfer system rules for clearing as between members for payment items ranging from cheques and bank drafts to electronic funds transfers.

At the provincial level, each province has many similar, parallel (and sometimes overlapping) regulatory authorities for matters within provincial legislative jurisdiction.

Territorial governments for Canada's three territories have been granted similar legislative powers as conferred on the provinces.

In addition to the host of laws, regulations and rules, touched on above, Canadian businesses of all sorts must comply with an array of privacy laws, both federal and provincial, Canada's anti-spam laws that limit and prescribe requirements for 'commercial electronic messages and competition laws that are aimed at ensuring fair and accurate marketing of financial products and services.

Financial institutions and those entities seeking to engage in financial services in Canada will require legal advice to ensure regulatory compliance for the jurisdictions engaged and the operations undertaken.

ii Structure of the courts

Each of Canada's 10 provinces has provincial superior courts with inherent jurisdiction and broad powers to administer law in their respective provinces. Appeals of the decisions of these courts are made to the respective provincial courts of appeal. In certain circumstances, the decisions of the courts of appeal may be further appealed to the Supreme Court of Canada, the highest court in Canada.

At the federal level, there is a parallel court system. The Federal Court hears and decides some disputes arising from federally regulated areas (i.e., federal administrative matters, intellectual property, privacy, income tax, immigration and maritime law). Its jurisdiction to

hear proceedings or to grant relief must specifically be found in a federal statute, such as the Federal Court Act, which must notably confer jurisdiction to the Federal Court in all cases in which relief is claimed against the government of Canada or federal administrative agencies.

iii Consumer protection legislation

Consumer protection provisions are contained in the federal Bank Act,² the Cooperative Credit Associations Act,³ the Insurance Companies Act,⁴ the Trust and Loan Companies Act⁵ and the Payment Card Networks Act.^{6,7}

The key Bank Act provisions (which apply to major Canadian retail banks) include disclosure provisions regarding charges and provisions governing retail deposit accounts,⁸ disclosure regarding borrowing costs associated with loans⁹ and credit cards,¹⁰ restrictions on tied selling¹¹ and the establishment of complaints resolution procedures.

Compliance with federal consumer protection procedures is overseen by the FCAC.

At the provincial level, each province has its own consumer protection legislation. In Quebec, for instance, the Consumer Protection Act¹² provides for several types of protection for consumers. On 15 November 2017, the government of Quebec adopted the Act, otherwise known as Bill 134 (the Bill), mainly to modernise rules relating to consumer credit and to regulate debt settlement service contracts, high-cost credit contracts and loyalty programmes, in order to modernise the Consumer Protection Act (Quebec). The Bill is set to come into force on 25 July 2019, except for certain provisions that will come into force in January 2019.

Consumer protection legislation are often the source of the complaints and proceedings by consumers against financial institutions.

II PROCEDURAL ISSUES

i Court procedures

The standard commercial litigation procedure is an 'action' in the superior court, culminating in a trial on documentary and oral evidence. The main steps in such an action are as follows. The plaintiff begins the action by filing and serving on the defendant a notice of civil claim or statement of claim, setting out its claim.

Generally, the subsequent step is discovery of documents. Each party must disclose to the other all documents within its possession or control that may relate to any issue in the action and that are not privileged. That is generally followed by examinations for discovery, which may require the attendance of the person being examined. Each party has the right to examine orally under oath one representative of the other about the issues in the action.

2 Statutes of Canada (SC) 1991, Chapter 46.

3 SC 1991, Chapter 48.

4 SC 1991, Chapter 47.

5 SC 1991, Chapter 45.

6 SC 2010, Chapter 12, Section 1834.

7 www.canada.ca/en/financial-consumer-agency/services/industry/laws-regulations/legislation.html.

8 Bank Act, Sections 439.1 to 447.

9 Bank Act, Section 450.

10 Bank Act, Section 452(1.1) and (2).

11 Bank Act, Section 459.1.

12 Revised Statutes of Quebec, Chapter P-40.

If that representative cannot satisfactorily inform themselves of the answers to questions beyond their personal knowledge, the party can apply for permission to examine a second representative in the same way.

Many other pretrial procedures are possible. For example, the parties may require answers by affidavit to written questions on issues in the action, called interrogatories. The parties may deliver notices to admit, requiring the admission of the truth of specific facts or of the authenticity of documents. Non-party witnesses who refuse to be interviewed can be examined under oath. Recorded or videotaped depositions of witnesses who cannot be required to appear at trial can be taken for use at trial.

Throughout the pretrial period, the parties may apply, on affidavit evidence, for interlocutory court orders resolving procedural issues, such as whether the pleadings should be amended, whether specific documents should be disclosed and whether specific questions asked on examination for discovery should be answered.

The action then goes to trial. Most commercial cases are tried by a judge, without a jury. The plaintiff presents its case first, calling witnesses to give oral evidence. The plaintiff's lawyer examines each witness and the defendant's cross-examines them. The defendant then calls its witnesses, and the plaintiff cross-examines them. The parties introduce documents into evidence either by agreement or through their identification by witnesses. The parties then present their legal arguments, based on the evidence introduced in the trial. The trial judge either makes a decision on the bench and gives oral reasons for judgment or, more likely, reserves his or her decision and gives written reasons for judgment several weeks to months later.

In most cases, the party that is unsuccessful at trial has an automatic right of appeal to the particular Court of Appeal. Generally speaking, to be successful in an appeal, a party must satisfy the Court of Appeal that the trial judge made an overriding error in interpreting or applying the applicable legal principle. Courts of appeal rarely interfere with factual findings of the trial judge.

The unsuccessful party in an appeal can seek leave to appeal further to the Supreme Court of Canada. Leave to appeal to the Supreme Court of Canada is rarely granted in commercial cases.

Summary procedures

In some circumstances, there are other procedural means of obtaining judgment in an expedited fashion. If a defendant does not file an appearance or response to civil claim, then judgment in default of appearance or summary judgment can be obtained a few weeks after that failure.

If the plaintiff can show, without introducing any evidence, that the defendant's notice of civil claim discloses no reasonable defence to its claim, the plaintiff can obtain a court order striking out the defence and granting it judgment.

A plaintiff can also obtain summary judgment if it can show, on affidavit, evidence that there is no triable issue in the action. This is a difficult test to meet.

The plaintiff can also apply for judgment by summary trial. A summary trial is a trial on the evidence in affidavits, the transcripts of examinations for discovery and documents, rather than on oral evidence. A summary trial is most likely to be successful where the important facts are not in dispute, or where factual disputes can be resolved on the basis of the evidence. If there are serious factual disputes, or if the parties' affidavits raise the credibility of witnesses, the court is not likely to allow a summary trial to proceed.

An application to strike out a statement of defence can be made at any time after the defence is filed. A summary judgment application can be made at any time after the defendant files an appearance. A summary trial application can be made at any time after the defendant files a statement of defence.

ii Limitation periods

Limitation periods may be prescribed by provincial laws or arise from enforceable contractual limitations that limit the time within which an action may be brought.

Generally speaking, most provincial limitation acts require that an action on a debt, such as one originating from an unpaid loan or promissory note, be begun within two or three years of the date on which the right to do so arose.

If material facts relating to the claim have been wilfully concealed (such as for fraud claims), some provinces have provisions that may extend the time for bringing suit. Typically, the extended limitation period does not begin to run until the identity of the defendant is known to the plaintiff and the facts within the plaintiff's means of knowledge are such that a reasonable person, knowing the facts and having taken the appropriate advice, would believe that an action would have a reasonable prospect of success (apart from the expiry of the limitation period) and that the plaintiff ought to be able to bring the action forward.

If the defendant confirms the cause of action against it before the limitation period expires, by acknowledging the claim or making a payment in respect of the claim, the limitation period begins anew from the time of the confirmation.

iii Class actions

Each province has its own legislative and procedural regime applicable to whether and how multiparty claims may be brought. There are many procedural similarities across the provinces and frequently, multi-jurisdictional class actions dealing with the same foundational claims will be coordinated by plaintiffs' legal counsel seeking to take advantage of the most advantageous legal and procedural jurisdiction for the claim being brought.

Quebec-based class actions and their criteria

When compared to the certification process in common law provinces, Quebec procedure is streamlined and designed to avoid lengthy contestations. In fact, Quebec is perceived across the country as a friendly forum for plaintiffs, as well as for the counsel acting on their behalf in class actions.

For example, the plaintiffs' motion for authorisation for certification does not have to be supported by an affidavit. For authorisation purposes, the facts alleged in the motion are deemed to be true and hearsay evidence is usually allowed (though its probative value may be limited). Moreover, the defendant can only contest the authorisation orally (i.e., without written pleadings) and must obtain the court's permission to present any evidence (e.g., deposition of the plaintiff or relevant documentary evidence). Finally, plaintiffs have a direct right of appeal if the authorisation is denied by the court of first instance; whereas the defendant, on the other hand, must obtain leave before appealing authorisation.

To be authorised, the proposed class action must satisfy the four cumulative criteria set out under Article 575 of the Code of Civil Procedure:

The court authorises the class action and appoints the class member it designates as representative plaintiff if it is of the opinion that:

- a the claims of the members of the class raise identical, similar or related issues of law or fact;*
- b the facts alleged appear to justify the conclusions sought;*
- c the composition of the class makes it difficult or impracticable to apply the rules for mandates to sue on behalf of others or for consolidation of proceedings; and*
- d the class member appointed as representative plaintiff is in a position to properly represent the class members.*

The burden is on the plaintiffs to show that the criteria are satisfied. That said, Quebec courts have set a low threshold for each criterion. Moreover, any doubt as to whether a criterion has been met will be resolved in favour of the plaintiff.

The first criterion will generally be met as long as the proposed action raises a single issue that is common to the class and is not negligible.¹³ The second criterion will be met if the plaintiffs can make out an ‘arguable case’ on a *prima facie* basis, no matter how slim the chances of success may be on the merits.¹⁴ The third criterion will commonly be met if there are at least a few dozen class members. As for the fourth and final criterion, a representative plaintiff should only be excluded if its interest or competence is such that the case could not possibly proceed fairly.¹⁵

Recent application by the court of the criteria

Through the recent case, *Asselin v. Desjardins Cabinet de Services Financiers Inc*, the Quebec Court of Appeal may have further lowered the threshold at the authorisation (certification) stage, by reversing once again a Quebec Superior Court decision that had refused to authorise a class action.

In doing so, the appellate court criticised the lower court judge for permitting the parties to present a fairly substantial evidentiary record, as it led to a more detailed analysis than what was appropriate at the authorisation stage. The judges should therefore evaluate whether the allegations meet a *prima facie* case and therefore avoid an in-depth analysis of the merits of potential grounds of defence.

A call for change in the industry: settlement process and class counsel fees

On 23 January 2017, the Superior Court of Quebec rendered an important judgment on settlement approval motions in four related class actions.¹⁶ The actions involved unilateral credit limit increases, over limit fees, cash advance fees and interest calculations, with plaintiffs alleging various violations of Quebec’s Consumer Protection Act. Similar or related

13 See *Vivendi Canada Inc v. Dell’Aniello*, 2014 SCC 1; *Sibiga v. Fido Solutions Inc*, 2016 QCCA 1299.

14 See *Infineon Technologies AG v. Option consommateurs*, 2013 SCC 59; *Charles v. Boiron Canada Inc*, 2016 QCCA 1716; *Sibiga v. Fido Solutions Inc*, 2016 QCCA 1299; *Asselin v. Desjardins Cabinet de Services Financiers Inc*, 2017 QCCA 1673.

15 See *Infineon Technologies AG v. Option consommateurs*, 2013 SCC 59; *Sibiga v. Fido Solutions Inc*, 2016 QCCA 1299.

16 *Option Consommateurs v. Banque Amex du Canada*, 2017 QCCS 200.

settlements with other banks had been previously approved for each cause of action involved. The Superior Court's decision to refuse approval of the proposed settlements came as a surprise to many.

In its review of the traditional seven criteria, the Court moved to refuse to approve the settlements largely based on the disproportion between the fees payable to class counsel and the compensation to be granted to members.

On 1 March 2018, the Court of Appeal dismissed the appeals and confirmed the decision of the Superior Court.¹⁷ The decision reiterates the important role of the courts to carefully review the fairness of any class action settlements, and that it is not bound in any way by their terms and conditions. As the approval of the legal fees by the Court was a pre-condition of validity and enforcement of the settlement agreements, the Court of Appeal confirmed that the Superior Court was constrained to refuse approving them.

III PRIVILEGE AND DISCLOSURE

The presumptive rule in Canadian litigation is that every document in the possession or control of a party must be produced, if it is relevant or material to a fact at issue, unless covered by some privilege. The actual test, whether 'relevance' or 'materiality', differs slightly across the provinces. In addition, entities that are not party to the litigation can be compelled to produce documents in their possession or control.

The most important exception to the obligation for the production of documents in the possession of parties jointly contemplating litigation arises from solicitor-client or litigation privileges. Such privileges allow the parties to seek legal advice in relation to the strengths and weaknesses of their case, strategies for pursuing or defending the claim and to conduct investigations in furtherance of the litigation, all without the obligation to disclose the documents created or the advice or information received. However, privilege can be lost or waived through disclosure of the documents, information or advice to parties outside of the directing minds of the relevant parties or through other means.

Solicitor-client privilege applies to communications between lawyer and client, including certain third parties as experts or agents. The communication must involve the giving or seeking of legal advice and must intend to be kept confidential. However, the communication doesn't need to relate to a 'specific' request for legal advice. Such privilege is permanent.

Litigation privilege applies to communication or documents that have been created or gathered for the 'dominant purpose' of litigation. The test of the dominant purpose requires that proceedings were a reasonable possibility at the time of communication and that the communication was made for that proceeding. One of the key differences with the solicitor-client privilege is that the litigation privilege ends with the litigation for which the documents were prepared, unless related proceedings ensue.

17 *Option Consommateurs v. Banque Amex du Canada*, 2018 QCCA 305.

IV FREQUENT CAUSES OF ACTION

Banks, financial institutions and other financial services providers are frequently the targets of litigation claims, all based on the confluence of potential for large value claims and the perception of ‘deep pockets’.

In Canada, the banker–customer relationship is fundamentally contractual. Historically, a contract governing a bank account consisted mainly of implied terms.¹⁸ Those terms were developed by the common law courts from the late 1600s onwards, and some of them were later codified in what is now the Bills of Exchange Act. Most bank account agreements are standard form contracts of adhesion. However, terms may still be implied.¹⁹

The banker–customer relationship is primarily one of debtor and creditor and is not fiduciary in nature. A fiduciary relationship arises only in special circumstances of vulnerability, duty and a reasonable expectation of paramount loyalty. It is the rare exception between a banker and customer that such a relationship ever arises. Further, the banker–customer relationship does not establish a trust over the funds on account. Simply put, under Canadian law, when a customer deposits money in an account at its bank, the customer is loaning money to the bank, and the bank becomes indebted to and obliged to repay the customer in accordance with the customer’s directions, subject to any defences that arise from the terms of the contract between the bank and customer.

As at 2018, cheques and other paper-based payment items remain common. Nearly a billion cheques are issued and processed in Canada each year.

The negotiation of cheques is governed by the Bills of Exchange Act. Banks commonly face claims relating to the misuse of cheques, including claims relating to cheque forgery, conversion, counterfeits, and material alterations.

i Forged signature (front of cheque)

A cheque is a direction to pay, written by the drawer or customer, directing the drawer’s banker to pay a sum certain to the payee.

When a cheque is issued by an individual, then it is a simple question of whether the drawer authorised or signed the cheque and whether they intended to have it issued. The question of forgery of the signature in these circumstances is a question of fact and not legally complex. If the signature on the cheque was forged, the item is a nullity, and then there is no actual mandate by the customer to their banker, and the banker is presumptively liable to its customer for paying on the cheque without mandate.

When a cheque is issued by a corporation, the simple question above becomes more complex. Who were the ‘authorised signatories’ of the corporation? Did the corporation intend to issue the cheque to the named payee or someone else?²⁰ What if an authorised signatory forges the signature of a second signatory when two must sign or causes a cheque to be issued to someone who is not owed money by the corporate drawer?²¹ Under Canadian bills of exchange law, these simple questions have led to some very complex law.²² The general rule remains that a forged signature of the drawer, with respect to a bill payable to

18 *Canadian Pacific Hotels Ltd v. Bank of Montreal* [1987] 1 SCR 711, 1987 CanLII 55 (SCC).

19 *BMP Global Distribution Inc v. Bank of Nova Scotia* [2009] 1 SCR 504; *Chriss v. The TD Bank Financial Group*, 2013 ONSC 7508 (CanLII).

20 *Teva Canada Ltd v. TD Canada Trust* [2017] 2 SCR 317, 2017 SCC 51 (CanLII).

21 *D2 Contracting Ltd v. The Bank of Nova Scotia*, 2015 BCSC 1634 (CanLII) 2016 BCCA 366 (CanLII).

22 *Canadian Pacific Hotels Ltd v. Bank of Montreal* [1987] 1 SCR 711, 1987 CanLII 55 (SCC).

order is a nullity that shifts the loss to the drawee bank, and yet the general rule is riddled with exceptions that flow from subtle factual differences that purport to the intentions of the drawer as a corporation or revert the loss back upon the corporate customer based on contractual preclusion defences.

ii Forged endorsement (back of cheque)

When a cheque is delivered from the drawer to the payee, the payee becomes the holder of the cheque. The cheque can then be further negotiated by endorsement, transfer or delivery. If negotiated for value, then the next party to the cheque becomes a ‘holder in due course’ with a presumptive right to enforce the cheque for payment. However, what happens when the endorsement of the payee has been forged? This simple question again has multiple answers, each of which depend on subtle differences between whether the endorsement was a necessary element for negotiation of the item. If the cheque was drawn to ‘order’, meaning a specific intended payee, then a forged endorsement breaks the chain of validity of negotiation and the parties to the cheque after the forged endorsement are presumptively liable for the tort of conversion.²³ In contrast, if the cheque was originally drawn to ‘bearer’, meaning it was drawn to a fictitious payee, then the endorsement by the payee was not necessary, and it is irrelevant that the endorsement was forged.²⁴

iii The tort of conversion

The strict liability tort of conversion is used to allocate losses for misappropriated cheques. A conversion is a wrongful interference with goods, such as by taking, using or destroying them in a manner inconsistent with the owner’s right of possession. To constitute the injury there must be some act of the defendant repudiating the owner’s right, or some exercise of dominion inconsistent with it. The wrongful act may be done in all innocence, but this is no defence. Any negligence on the part of the drawer or the banks in preventing the fraud is irrelevant.²⁵

This tort claim is a common method by which to allocate cheque fraud losses up to the collecting bank or to any other parties that negotiated the cheque after the item was issued. There are a few limited defences to these types of claims,²⁶ but under Canadian law (unlike UK legislation) contributory fault of the drawer is not a basis for apportionment of the loss.²⁷

iv The tort of knowing receipt

The cause of action in knowing receipt arises simply because the defendant has improperly received property that belongs to the plaintiff. This type of claim remains common against financial institutions on the asserted basis that the bank has received funds that were fraudulently taken from an innocent victim. The plaintiff’s claim amounts to nothing more than, ‘You unjustly have my property. Give it back’. Unlike the similarly named tort of ‘knowing assistance’, there is no finding of fault, no legal wrong done by the defendant and no claim for damages. It is, at base, simply a question of who has a better claim to the disputed

23 *Boma Manufacturing Ltd v. Canadian Imperial Bank of Commerce* [1996] 3 SCR 727, 1996 CanLII 149 (SCC).

24 *Fok Cheong Shing Investments Co Ltd v. Bank of Nova Scotia* [1982] 2 SCR 488, 1982 CanLII 57 (SCC).

25 *Arrow Transfer Company Ltd v. Royal Bank of Canada et al* [1972] SCR 845, 1972 CanLII 135 (SCC).

26 *National Holdings Ltd v. CIBC et al*, 2005 BCSC 369 (CanLII).

27 *GE Capital Canada v. Bank of Montreal*, 2003 BCSC 1180 (CanLII).

property. In order to recover the disputed property, the plaintiff must prove the following: (1) that the property was subject to a trust in favour of the plaintiff; (2) that the property, which the defendant received, was taken from the plaintiff in breach of trust or breach of fiduciary duty; and (3) that the defendant did not take the property as a *bona fide* purchaser for value without notice. The defendant will be taken to have notice if the circumstances were such as to put a reasonable person on inquiry, and the defendant made none, or if the defendant was put off by an answer that would not have satisfied a reasonable person.

Claims of this nature are brought against banks and other financial service businesses on the basis that they were or should have been put on notice about the suspicious circumstances by which the bank's customer delivered funds and that the bank failed to investigate owing to negligence or wilful blindness. A proliferation of Ponzi scheme claims have used this legal theory against banks to advance claims for the victims of the scheme, yet very few claims have successfully demonstrated bankers' liability for such.

v Customer impersonation – misdirected payments

Cheques and the law of bills of exchange evolved in an era when 'banks were taken to know the signature of their customer'. Thus, it was reasonable that the presumptive loss allocation for forged signature was directed at the drawer's bank for paying without mandate and that the loss allocation for forged endorsement situations flowed to the collecting bank that allowed itself to deal with a rogue. In contrast, the world of payments and banking has evolved considerably with mobile payments, internet banking and the expectation of 24/7 financial access, anywhere, anytime. As payment systems have evolved to meet customer expectations, customer safety and security for their personal access devices, and the modes used to instruct the bank, have become a target for identity thieves, whether by hacking, phishing, sniffing or stealing the devices used. In consequence, customer losses and claims against banks are on the rise in relation to said evolving issues.

In one recent claim scenario, a bank customer sued his bank for losses owing to fraudulent email instructions that caused a wire transfer to be issued to his detriment. The terms of the application and the account agreement entitled the customer to provide instructions to his bank by email address and the customer previously did so without complaint to effect a wire transfer. The bank was contractually entitled to rely on those instructions. The customer had the sole ability and responsibility to control the security of the email account that was the source of the impugned instructions, yet the customer's email account was hacked and fraudulent instructions were issued. The court held that the contractual exclusions in favour of the bank were valid, that the bank had not been grossly negligent by failing to follow up and enquire of the instructions and as such allocated the loss to the customer.²⁸

While the loss allocation in *Du* is supportable on the circumstances of the case, this decision further illustrates the importance of ensuring clear, unambiguous terms and conditions in the customer account agreement. A well drafted account agreement that defines and limits the mutual expectations for fraud prevention, detection and allocation will go a long way to limit losses owing to claims.

28 *Du v. Jameson Bank*, 2017 ONSC 2422 (CanLII).

vi Privacy and data breach

Canadian financial institutions have long had traditional duties of customer confidentiality for personal information. The obligations for customer confidentiality are now further codified in legislation, such as the Personal Information Protection and Electronic Documents Act, applicable to federally regulated institutions (i.e., banks), and at the provincial level by substantially similar provincial laws where such are enacted. They set out principles regarding how organisations must handle the collection, use and disclosure of personal information in the course of their commercial activities. The overarching principle is that collection, use and disclosure of personal information collected by financial institutions in respect of customers requires the consent of the individual except in narrowly defined circumstances set forth in the legislation.

V LIMITATIONS ON LIABILITY

In both common law and civil law, courts have recognised that an explicit and clear stipulation to exclude liability of the financial institution is valid when such stipulation specifies the acts for which an exoneration applies. Such clauses are normally interpreted restrictively by courts, against the financial institution, but always in a manner that best reflects the common intention of the parties.

In the context of fraudulent signatures, for example, banks are deemed to know the signature of their clients and are responsible for all unauthorised payments made from a cheque on which the signature has been forged. Nonetheless, courts have frequently recognised the validity of agreements requiring the customer to verify the signature of the cheques signed or to notify the bank of any erroneous debits within a certain delay.²⁹

VI LOOKING AHEAD

Canadian business leaders are facing an economy that is increasingly complex and unpredictable. They are not only affected by the policies of Canada's federal and provincial governments, but also by international changes, such as the rise of populism and protectionism. This combination is bound to raise the level of uncertainty for all businesses. Trade agreements, cross-border commerce and the market implications of legalising cannabis are, for instance, topics that may have serious impacts on the Canadian economy.

As for the topics covered above, it remains that all signs indicate that the trend of litigation and of class actions becoming more common and broader in scope will continue. With large-scale data breaches dominating headlines, expect to see numerous proceedings aimed at financial institutions related to privacy and cybersecurity issues.

²⁹ *Arrow Transfer Company Ltd v. Royal Bank of Canada et al* [1972] SCR 845; *Productions Mark Blandford Inc v. Caisse populaire St-Louis de France*, 2000 CanLII 10274 (CA); *Aliments C&C Inc v. Banque Royale du Canada*, 2014 QCCA 1578.

FRANCE

Arnaud de La Cotardière and Jean-Charles Jaïs¹

I SIGNIFICANT RECENT CASES

i Annual percentage rate of charge

The requirement of the mention of an accurate annual percentage rate of charge (TEG) in a loan agreement is a mandatory feature imposed both to protect the borrower and to promote transparency. The absence or inaccuracy of the annual percentage rate indicated in a loan agreement is a recurring theme raised against banks by borrowers in an attempt to reduce the cost of their loan.

The sanction attached to such irregularities varies according to the type of contract at stake and may consist either in the negation, in full or in part, of the bank's right to interest, or in the substitution of the – in practice significantly lower – legal interest rate to the TEG. Every year, case law provides for a further development or clarification on the subject.

The Supreme Court recently ruled that, in relation to loans granted to a consumer or a non-professional, the sanction of the inaccuracy of a TEG, resulting from the application of an interest rate based on 360 days rather than the calendar year, is the substitution of the legal interest rate to the TEG.²

The Supreme Court also recently upheld that, in the case of a consumer loan, a mistake in the TEG stipulated contractually needed to exceed at least one decimal point to be sanctioned.³ A first instance court, however, referred a question to the Court of Justice of the European Union for a preliminary ruling, to ask whether French case law allowing for a decimal point mistake was contrary to European law.⁴ Depending on the Court's answer, this leniency may or may not last.

ii Indexation clauses

Structured loans have been offered on the French markets to individuals who borrowed an amount in Swiss francs to be reimbursed in euros. In 2015, the Swiss Central Bank ceased to defend the previous 1.20 Swiss franc-euro parity, which resulted in a rise of the cost of the loan for the borrowers. The subsequent disputes have been largely publicised.

1 Arnaud de La Cotardière and Jean-Charles Jaïs are partners at Linklaters LLP. The authors are grateful to Hubert Delerive for his research and assistance in the preparation of this chapter.

2 Cass. Com., 29 November 2017, No. 16-17.802.

3 Cass. Com., 18 May 2017, No. 16-11.147.

4 Limoges First Instance Court, 11 October 2017, No. 17-000561.

The first two decisions of the Supreme Court on the subject were rendered on the same day. The Court ruled on the validity of indexation clauses providing for a revision of the interest rate depending on the variation of the exchange rate between the euro and Swiss franc.⁵ The Supreme Court considered such clause could constitute an unfair contract term and that the judges therefore ought to examine whether the risk is exclusively borne by the borrower and whether, consequently, the disputed clause has the object or effect of creating a significant imbalance between the rights and obligations of the parties to the detriment of consumers.

The Court of Appeal of Paris has, however, recently changed its position,⁶ followed by the Supreme Court.⁷ In these last rulings, the validity of such indexation clauses depends on their clarity and comprehensibility. For example, in the case ruled by the Court of Appeal of Paris, the clarity and comprehensibility of the clause was assessed in light of a notice provided by the bank and that illustrated the consequences of the variation of the exchange rate with quantified examples. The Court concluded that the borrower had therefore been clearly informed of the characteristics of the contract.

This new case law is consistent with the line given by the Court of Justice of the European Union in its case C-186-16 dated 20 September 2017, which considered, in substance, that a loan denominated in a foreign currency and providing for repayment in the same foreign currency is not abusive, provided that the related clauses are drafted in a clear and comprehensible manner.

iii Banks' duties

The duties of a bank towards its client (to inform, to advise, to warn, to care and not to intervene) are a recurring theme in litigation and recent case law continues to shed additional light on those various duties.

For instance, the Supreme Court recently ruled that a bank did not breach its duty to advise by failing to verify the authenticity of the documents related to its client's financial capacity, since there were no apparent anomalies.⁸

In another case, the Supreme Court dealt with the scope of the bank's duty to advise its client. In principle, a bank granting a loan is not bound by such a duty by mere virtue of the fact that it is lending funds and does not have to judge the appropriateness of the requested credit. Such a duty and related liability may, however, arise where a bank provides specific recommendations when granting a loan. For instance, in a decision dated 7 February 2018, the Supreme Court held that the bank had issued advice insofar as it was at the initiative of the latter, which acknowledged having been aware of the company's difficulties and the purpose of the loans, that such loans were granted to the borrower in a personal capacity with express stipulation of allocation to the profit of the company.⁹

iv Statute of limitation

The statute of limitation with regards to the TEG, in the context of a loan agreement entered between professionals, has given rise to abundant case law in recent years.

5 Cass. Civ. 1, 29 March 2017, Nos. 15-27.231 and 16-13.050.

6 Paris Court of Appeal, 6 October 2017, No. 16-03076.

7 Cass. Civ. 1, 3 May 2018, No. 17-13.593.

8 Cass. Civ., 1, 5 July 2017, No. 16-17.103.

9 Cass. Com., 7 February 2018, Nos. 16-12.808 and 16-24.004.

On the one hand, according to the First Civil Chamber of the Supreme Court, the starting point of the limitation period is either the date of the agreement when examination of its content revealed an intrinsic error or, where that is not the case, the date on which the error is revealed to the borrower.¹⁰ On the other hand, the Commercial Division of the Supreme Court adopted a different solution. Indeed, it usually considers that the limitation period should run from the date of the agreement, which was deemed to be the date on which the borrower had known or should have known the defect affecting the TEG.

In January 2017, this difference appeared to be called into question by a decision of the Commercial Division. In the latter case, this Division considered that the starting point was ‘the day on which the borrower had known or should have known the defect affecting the rate’, but without referring to the date of the agreement.¹¹ Some authors had considered this decision to be a reversal.

In a decision dated 4 May 2017, the Commercial Division, however, confirmed its historical position by finding that ‘the starting point of this limitation period is the date of the loan agreement mentioning the allegedly erroneous rate’.¹² A professional is supposed to be able to detect the erroneous nature of the TEG as of the day of the loan agreement. This new decision confirms the divergence between the First Civil Chamber and the Commercial Division.

v **Banking secrecy**

Article 145 of the French Code of Civil Procedure authorises *in futurum* investigation measures in the context of civil disputes, while Article 11 of the same Code provides for an exception where there exists a legitimate impediment to such measures.

Whereas banking secrecy usually impeded any disclosure of documents or information for purposes of *in futurum* investigation measures, the Supreme Court recently created a distinction as to whether the bank to whom the request for communication is addressed is taken as a third party, or as a party to the proceedings brought against it. In a decision dated 29 November 2017, the Court made it possible to lift the banking secrecy, in order to determine the liability of the bank in the disputed transaction, when the bank is to be a party to the proceedings on the merits.¹³

II **RECENT LEGISLATIVE DEVELOPMENTS**

i **Contract law reform**¹⁴

It is not possible to summarise the entire impact of this reform in the context of this chapter. Nevertheless, the following are some of the innovations that concern the banking sector:

- a the reinforcement of the enforceability of unilateral promises that had been undermined by previous case law in comparison to other pre-contractual instruments (offers and pre-emption agreements);

10 See, for a recent example, Cass. Civ. 1, 1 March 2017, Nos. 15-16819 and 16-10270.

11 Cass. Com., 31 January 2017, No. 14-26.360.

12 Cass. Com., 4 May 2017, No. 15-19.141.

13 Cass. Com., 29 November 2017, No. 16-22.060.

14 Order No. 2016-131 dated 10 February 2016 on the reform of contract law, and of the general regime and proof of the obligations. The new law entered into force on 1 October 2016 and was ratified on 20 April 2018 by Law No. 2018-287, which will enter into force on 1 October 2018.

- b* the introduction, in French contract law, of the notion of unfair contract terms that were only present in specific legislation (consumer law). The possibility to declare such provision null and void is now provided for in the context of standard form contracts and in the case of significant imbalance between the rights of the parties;¹⁵
- c* the introduction of assignment of contracts and debts, and the new provisions on novation and subrogation;
- d* the exploitation of the other party's dependence in the context of the entry into the agreement is deemed to constitute an act of duress voiding the agreement under certain conditions (i.e., the party's state of dependence was the only reason it entered into the agreement and the advantages obtained from the dependent party are manifestly excessive);¹⁶ and
- e* the modification of the frustration of purpose regime, which introduces a possibility for a court, under certain circumstances, after certain steps have been taken and absent contrary provisions, to revise a contract or put an end to it.¹⁷

ii Sapin II law

The law known as Sapin II introduced a new legislative framework related to the fight against corruption that will have an impact on the banking and financial sector.¹⁸ The law provides for an obligation to put in place internal measures and procedures in order to prevent and detect corruption and trading in influence actions. Eight different types of measures that had to be put into place by 1 June 2017 are: (1) a code of conduct; (2) an internal reporting procedure; (3) risk mapping; (4) evaluation procedures for clients, suppliers and intermediaries; (5) internal and external accounting control procedures; (6) a training system; (7) a disciplinary sanction regime; and (8) an internal evaluation and control system.

The law also creates an anticorruption agency with sanctioning powers (of up to €1 million in pecuniary sanctions) to control compliance with the new obligations and provides for new reporting procedures before the Financial Markets Authority (the financial

15 Article 1171 Civil Code: 'Any term of a standard form contract which creates a significant imbalance in the rights and obligations of the parties to the contract is deemed not written. The assessment of significant imbalance may not concern neither the main subject-matter of the contract nor the adequacy of the price in relation to the act of performance.' Standard form contracts are defined at Article 1110 of the Civil Code as follows: 'A standard form contract is one whose general conditions are determined in advance by one of the parties without negotiation.'

16 Article 1143 Civil Code: 'There is also duress when one contracting party exploits the other's state of dependence and obtains an undertaking to which the latter would not have agreed in the absence of such constraint, and gains from it a manifestly excessive advantage.'

17 Article 1195 Civil Code: 'If a change of circumstances that was unforeseeable at the time of the conclusion of the contract renders performance excessively onerous for a party who has not accepted the risk of such a change, that party may ask the other contracting party to renegotiate the contract. The first party must continue to perform his obligations during renegotiation.

In the case of refusal or the failure of renegotiations, the parties may agree to terminate the contract from the date and on the conditions which they determine, or by a common agreement ask the court to set about its adaptation. In the absence of an agreement within a reasonable time, the court may, on the request of a party, revise the contract or put an end to it, from a date and subject to such conditions as it shall determine.'

18 Law No. 2016-1691 dated 9 December 2016 relative to transparency, fight against corruption and modernisation of the economic life.

regulator) and the Prudential Supervision and Resolution Authority (the supervising authority for the banking and insurance sectors) for a lack of compliance with European or French provisions in the financial sector.

The Sapin II law contains a variety of provisions on several different topics. In addition to the above, another subject of interest in the banking sector is the provisions modifying the hierarchy of the creditors of credit institutions in case of winding-up proceedings by creating a new category of bonded debt.¹⁹ This modification aims at facilitating bail-in by adding a new class of assets that will absorb the debt and constitute an extra layer of protection for the simple savers. Some banks have already tested this new tool.²⁰

The law was completed by Decree No. 2017-892 dated 6 May 2017 that enacts different measures, among which some provisions related to enforcement proceedings.²¹

Besides, the law introduced the possibility to conclude a financial settlement, known as a judicial public interest agreement,²² for the benefit of companies that are accused of certain offences,²³ as long as the public action has not been initiated.²⁴ The terms and structure of this settlement bear many similarities to deferred prosecution agreements that are entered into in the United States. After approval by the public prosecutor, the proposal is submitted to the President of the District Court (Tribunal de grande instance) for validation.

The first settlement entered into between the public prosecutor and a bank was approved by the District Court of Paris on 14 November 2017, under which the bank agreed to pay a total of €300 million to settle offences relating to money laundering and tax evasion.²⁵

In June 2018, another bank also entered into a judicial public interest agreement with the French prosecution authority that puts an end to the latter's investigations into transactions involving Libyan counterparties. As part of this settlement, the bank has agreed to pay penalties totalling approximately €250 million. The bank has also committed to ensuring that its internal policies, procedures and controls are designed to prevent and detect violations of the relevant anti-bribery laws.²⁶ A similar agreement has been entered into with the US Department of Justice. This is the first coordinated resolution between US and French authorities in a bribery case.

iii Recent regulatory texts

A number of regulatory texts adopted in 2017 and 2018 had an impact on the banking sector, notably:

- a* Law on the reform of contract law and the general regime and proof of the obligations, which ratifies Order No. 2016-131 dated 10 February 2016;
- b* Order No. 2017-1674 dated 8 December 2017 allowing the use of blockchain for title transfers;

19 Article 151 Sapin II law, modifying Article L.613-30-3 of the Monetary and Financial Code.

20 'French banks test the 'Sapin II' debt', *Les Echos*, 15 December 2016.

21 See Section IV, below.

22 *Convention judiciaire d'intérêt public*.

23 Such as bribery or influence peddling offences, as well as tax laundering offences.

24 Article 41-1-2 Code of Criminal Procedure.

25 District Court of Paris, 14 November 2017, No. PNF 11 024 092 018.

26 District Court of Paris, 24 May 2018, No. PNF 15 254 000 424.

- c* Decree No. 2017-1094 dated 12 June 2017 and the related Decree No. 2018-284 dated 18 April 2016 relative to beneficial owners, which compels registered legal entities to file a document regarding their beneficial owners, and therefore allows for determination of who ultimately controls said legal entity;
- d* Decree No. 2017-892 dated 6 May 2017 providing for diverse measures of modernisation and simplification of civil procedure; and
- e* Decree No. 2017-888 dated 6 May 2017 relative to class action provided for in Law No. 2016-1547 dated 18 November 2016 on the modernisation of justice in the 21st century.

III CHANGES TO COURT PROCEDURE

i Appeal procedure reform

A recent decree modified the rules relative to proceedings before the courts of appeal.²⁷ Most rules of the appeal procedure reform apply to rulings or appeals lodged after 1 September 2017. The new rules in particular simplify challenges to jurisdiction, refocus appeal proceedings on the criticism of the first instance judgment, introduce strong concentration principles, regulate procedural delays and require greater formalisation of acts.

ii International aspects of recent procedural changes

Another recent decree brought several changes to various procedural issues,²⁸ including the reform of the regime of international letters rogatory in several aspects. The most interesting change relates to the possibility for a foreign judge to directly carry out (via videoconference) the hearing of a person it requested, concerning letters rogatory delivered under The Hague Convention and under certain circumstances.²⁹ In addition, it institutes the exclusive jurisdiction of the District Court and provides for the existence of a special judge in charge of supervising the execution of the letters rogatory.

An international chamber has recently been created within the Court of Appeal of Paris.³⁰ It has jurisdiction to rule on appeals of decisions delivered in international commercial disputes, and in particular disputes that involve provisions of European or foreign law. In this respect, it is sufficient that one of the parties is a foreign entity or that a foreign law is applicable to trigger the special chamber's jurisdiction. The chamber's jurisdiction may also result from a jurisdiction clause.

The English language can be used during the proceedings. Even if pleadings and judgments are still drafted in French, documents in English may be filed without translation and judgments are translated under the responsibility of the court's registrar. In addition, if

27 Decree No. 2017-891 dated 2 August 2017 amending the terms of entry into force of Decree No. 2017-891 dated 6 May 2017 relative to the lack of jurisdiction pleas and appeal in civil matters; Circular No. JUSC1721995C dated 4 August 2017 presenting the provisions of this Decree.

28 Decree No. 2017-892 dated 6 May 2017 adopting various measures of modernisation and simplification of civil procedure.

29 New Article 747-1 Code of Civil Procedure: 'If it is requested in the rogatory letter, and as far as the measure of inquiry solely provides for a hearing, the Ministry of Justice can authorise its direct performance by the foreign court, notably via videoconference, without any possible constraint or penalty.'

30 Protocols relating to proceedings before the International Chamber of the Court of Appeal of Paris and First Instance Court of Paris dated 7 February 2018.

the proceedings are to be held in French, simultaneous translation by a translator appointed by the court may be arranged. Parties appearing before the judge, witnesses and technicians, including experts, when they are foreigners, may speak English if they so wish.

Moreover, the possibility to use certain mechanisms akin to those of common law, such as cross-examinations, appears to have been introduced in theory. Their practical implementation, however, remains to be seen in practice.

iii Class action

Following the introduction in 2014 of the French equivalent of the class action, note that, of the 12 actions initiated since then, several concern the banking sector. For instance, in March 2018, an action was filed against Natixis, following a fine imposed by the Enforcement Committee of the French Financial Markets Authority.³¹

IV INTERIM MEASURES

The only major recent change in relation to interim measures concerns proceedings relating to assets belonging to foreign states. Sapin II, the anti-corruption law,³² introduces several provisions regarding enforcement proceedings – including interim measures – against assets belonging to a foreign state located on French soil, partially codifying the previous regime. The law introduces a prerequisite according to which provisional and enforcement measures against an asset belonging to a foreign state now require a prior judicial authorisation.³³ The law codified the following scenarios in which such measures are possible: (1) the state expressly consented to the application of such measure; (2) the state allocated or earmarked the property for the satisfaction of the claim that is the object of the proceedings; and (3) where a judgment or an arbitral award was rendered, the property is specifically in use or intended for use by the state for purposes other than government non-commercial and it has a connection with the entity against which the proceeding was directed. Moreover, the new Article L.111-1-3 of the Code of Civil Enforcement Proceedings clarifies the conditions under which a state can waive immunity from execution on property necessary to the diplomatic activity. This new Article supersedes the latest case law,³⁴ which abandoned the requirement that the waiver be specific (i.e., that it established the list of the goods susceptible to be seized).³⁵

V LAWYER-CLIENT PRIVILEGE

i Definition and scope

The relationship between a lawyer (admitted to the local Bar) and his or her client is protected by the general professional secrecy obligations set out in Article 226-13 of the Criminal Code that prohibit a professional who is subject to a secrecy obligation from divulging information

31 Enforcement Committee, 25 July 2017, SAN-2017-07.

32 See Section II.ii, above.

33 Article R.111-1 Code of Civil Enforcement Proceedings.

34 Cass. Civ. 1, 13 May 2015, No. 13-17.751.

35 On this subject, see J Heymann, *JCP G* No. 5, 30 January 2017, 102, who notably questions the conventionality of the new judicial authorisation prerequisite and of the necessity of an express and specific waiver of immunity from execution for diplomatic property.

obtained from the client. The client is not, however, bound by this secrecy obligation. In addition, Article 66-5 of the Law of 31 December 1971 on the status of lawyers provides that any written communication addressed by a lawyer to his or her client (correspondence, meeting notes and generally all documents forming part of the client's file) and by a lawyer to another lawyer in relation to a matter handled on behalf of a client, are protected by professional secrecy (unless expressly indicated to the contrary in the latter case). A client cannot release his or her lawyer from the obligation to keep all of these documents confidential.

ii In-house lawyer

The concept of in-house lawyer privilege is not recognised in France. In-house lawyers may not retain their lawyer status and they may not represent their employers in proceedings where representation is compulsory.

iii Application by the courts and public authorities

In civil and commercial matters, the doctrine of privilege is binding and respected by regulatory and other investigative bodies. Regulatory bodies (e.g., competition and financial authorities) cannot order the production of, or rely upon, documents protected by professional secrecy while investigating and carrying out checks.

In criminal, customs and tax matters the position is slightly different. In theory, documents protected by professional secrecy cannot be seized during searches conducted by the investigating magistrate. Nor can they be removed by regulatory and public bodies (competition and financial authorities, customs and tax) when they undertake court-authorised premises searches. Documents may only be seized when the search is intended to collect evidence of a criminal offence or certain customs and tax offences. This prohibition of seizure extends to lawyer-client communications held at the client's premises.

The Code of Criminal Procedure sets out one exception to the rules on professional secrecy in relation to lawyers' documents and objects (such as mobile phones, laptops, etc.). They are no longer protected by professional secrecy when they are seized as evidence of a lawyer's commission of a criminal offence or certain customs and tax offences. If the seizure is made at the domicile or office of a lawyer the search may only be carried out by a judge and the Head of the Bar Association, or his or her delegate must be present during the search. In addition, the Criminal Chamber of the Supreme Court reconfirmed the distinction drawn between documents relating to the exercise of the defence rights and documents relating to the drafting and negotiating activities of a lawyer; documents that are not related to the exercise of defence rights can be seized if it is necessary for ascertaining the truth and on condition that the breach of professional confidentiality is strictly proportionate.

Finally, as a result of a recent law,³⁶ the access to and the copying of a lawyer's electronic mailbox can be authorised by a specialised judge, following a simple notification to the President of the Bar, for the purposes of an inquiry relative to organised crime offences if the lawyer is suspected to have taken part in the offence. In addition, the new provisions specify that the fact that the authorised operations revealed offences different from those identified in the judge's authorisation does not constitute a reason to invalidate incidental proceedings.

³⁶ Law No. 2016-731 dated 3 June 2016 reinforcing the fight against organised crime, terrorism and their financing and improving the efficiency and the guarantees of criminal procedure.

VI JURISDICTION AND CONFLICTS OF LAW

The Supreme Court recently decided to extend an arbitration clause to a banker who was not a signatory of the clause, but became, through a factoring agreement, the owner of the receivables held by one of the signatories of the arbitration clause.³⁷ An author recently noted in this respect that ‘in practice, it will be almost impossible for a bank which acts as a transferee bank for the benefit of its client to avoid the arbitration clause contained in the commercial contracts from which the receivables transferred to it (through a factoring agreement or a “Dailly Assignment”) originate’.³⁸

Besides, the Supreme Court confirmed that French texts governing banking secrecy were applicable in the context of bankruptcy proceedings governed by Cayman Islands law. The Court considered that the mission of the liquidator of the Cayman Islands, applicant at hand, was similar to that of French liquidators, and as a consequence that French rules regarding suspension of banking secrecy could apply, the bank in case being established in France.³⁹

VII SOURCES OF LITIGATION

The current main sources of litigation against banks have been outlined in Section I, above. Ongoing litigation involving banks notably revolves around the compliance of banks with their various duties in the context of loans or commercialisation of financial products. Other subjects that remain topical are the interest rate, as well as validity and enforceability of a guarantor’s undertakings.

VIII EXCLUSION OF LIABILITY

Limitation of liability clauses are not enforced in case of wilful misconduct or gross negligence. The order reforming French contract law⁴⁰ codified a further exception to the validity of exemption clauses previously developed by case law. The new Article 1170 of the Civil Code provides that contract terms that deprive a debtor’s essential obligation of its substance is deemed null and void. An exemption clause should not make the execution of the contract meaningless. This means in practice that the clause should not establish a liability threshold so high that it would in fact never be reached and should not fix a compensation too low. This situation will be assessed by French courts on a case-by-case basis.

As for previous case law, there is the question of what use could be made of the above provision against investment banks in the context of M&A deals. It is typical for a client to hold harmless an investment bank against any action that a third party may initiate against the bank in relation to a deal. In relation to limitation of liability clauses this coverage is typically excluded in case of wilful misconduct or gross negligence of the bank. It is arguable that, in certain circumstances, Article 1170 of the Civil Code could apply to this warranty as well.

37 Cass. Civ. 1, 13 September 2017, No. 16-18178.

38 J Morel-Maroger, *Banque & Droit* No. 177, January–February 2018, p. 38.

39 Cass. Com., 29 November 2017, No. 16-22.060.

40 See Section II.i, above.

IX REGULATORY IMPACT

The proliferation of norms in the banking and financial sector bears the correlative risk for banks of new litigation based upon their lack of compliance with such regulations. Banks are subject to an increasing number of obligations relative to anti-money laundering and terrorist financing. In particular, suspicious transactions must be reported to Tracfin.⁴¹ In a recent decision of the Prudential Supervision and Resolution Authority, a bank was given a €5 million administrative fine considering the time taken by the latter to report suspicious transactions, the lack of internal control within the bank and the failure to report some transactions.⁴²

X LOOKING AHEAD

No major French laws concerning the banking sector are currently expected.

A piece of draft legislation is being prepared that provides for the removal of the mandatory mention of the annual percentage rate of charge in the loans to professionals.⁴³ It also seeks to clarify and standardise the sanctions regime in case of absence or inaccuracy of the TEG in a consumer loan.

In addition, France seeks to endorse a legislative framework for the use of blockchain and will be the first European country to do so. Indeed, an order has already been passed to allow the use of blockchain for securities transfers.⁴⁴

41 Tracfin is a public agency that fights against illegal financial circuits, money laundering and the financing of terrorism.

42 Enforcement Committee of the Prudential Supervision and Resolution Authority, 19 July 2017, No. 2016-07.

43 Draft Law for a State at the service of a society of trust, adopted by the National Assembly and the Senate at first reading on 20 March 2018, but returned to the National Assembly for a new reading owing to a disagreement within the Joint Committee.

44 Order No. 2017-1674, 8 December 2017, JO 9 December 2017.

GERMANY

*Christian Schmitt*¹

I SIGNIFICANT RECENT CASES

Following the financial crisis, the German Federal Court of Justice (BGH) adjudicated several important cases in the area of banking litigation.

i Contractual close-out netting and statutory insolvency law

In 2016, the BGH rendered a judgment with wide-ranging implications regarding contractual close-out netting.² It held that contractual close-out netting rules are invalid insofar as they contradict statutory netting claims (Section 104 of the German Insolvency Code). Consequently, the statutory rules are directly applicable, protecting the insolvency estate. This aim was threatened in the court's view by the possibility of contractual close-out netting claims being calculated differently than under the statutory regime.

The judgment received wide attention and the German Federal Financial Supervisory Authority reacted immediately by a general decree stating that contractual close-out netting clauses continued to be valid. A fast-tracked legislative proposal was passed in December 2016 that provides legal certainty on the requirements for contractual close-out netting rules and updates the statutory provisions on several issues (e.g., valuation methods).

ii Notable cases dealing with conflict of interest scenarios before the German courts

In recent years, two different series of judgments have influenced banking law practice in Germany significantly. On the one hand, the 'kickback' proceedings series deals with the important obligation of the investment adviser to disclose kickbacks from the issuer to the investment adviser. This is particularly relevant in the retail customer business.³ Until the most recent judgment in this series, the BGH used to differentiate commission payments by third parties from internal commission payments paid out of the investment capital. These were not subject to a duty of disclosure unless they amounted to 15 per cent or more of the investment capital.⁴ Following a change in the law, this distinction has now been rendered superfluous: from 1 August 2014, a duty of disclosure applies to all commission payments.

1 Christian Schmitt is a partner at Linklaters LLP. The author would like to thank associates Martin Bär and Tobias Bastian, as well as legal assistant Benedikt Heil, for their invaluable support in the preparation of this chapter.

2 BGH, judgment of 9 June 2016, court reference: IX ZR 314/14.

3 BGH, court order of 29 June 2010, court reference: XI ZR 308/09.

4 BGH, judgment of 23 June 2016, court reference: III ZR 308/15.

On the other hand, the BGH delivered a series of judgments on the obligation to disclose to the counterparty a negative market value at the beginning of the duration of a derivative. This series of judgments began with the Court's 2011 *Ille* judgment and moved on to derivative transactions concluded with German municipalities. In 2015, the Court handed down two decisions that clarified (1) the expression 'negative market value' and (2) the scope of applicability of such obligations (i.e., whether the exception of a 'connected hedging transaction' exists, which means that no disclosure obligation applies). In 2016, the Court set out the requirements of a 'connected hedging transaction'.⁵ The BGH also recently called to mind the prohibition of financial speculation for German municipalities. It lifted the acquittal of a municipal official who was accused of embezzlement because he authorised speculative trades.⁶

II RECENT LEGISLATIVE DEVELOPMENTS

i **European Account Preservation Order – Regulation (EU) No. 655/2014 of the European Parliament and of the Council of 15 May 2014**

The European Account Preservation Order (EAPO) is a European instrument similar to an English worldwide freezing order. As an alternative to preservation measures under national law, it aims to ensure the enforcement of an existing or a future judgment. It preserves the *status quo*.

The EAPO applies to pecuniary claims in civil and commercial matters in cross-border cases that are specified in Article 3(1) of Regulation (EU) No. 655/2014 (the Regulation) (when either the bank account and creditor or the bank account and the court that issues the EAPO are in different Member States of the European Union). It targets debtors who are likely to thwart the enforcement of such judgment by transferring or withdrawing the funds by preserving the debtor's bank account. The debtor is generally not notified about the EAPO proceedings, therefore an EAPO can make use of the surprise effect – contrary to proceedings with mutual recognition in which the debtor or defendant is necessarily heard. Pursuant to Article 6 of the Regulation, jurisdiction for an EAPO normally lies with the court of the main proceedings.

If no prior judgment exists, the court examines the claim's chance of success before granting an EAPO. As well as the EAPO, according to Article 14 of the Regulation, there is the possibility to request information about the debtor's bank accounts in order to find out where funds that could be seized, exist.

ii **Markets in Financial Instruments Directive Inducement Rules and Fee-Based Investment Advice Act**

Similar to the conflict of interest cases adjudicated by the BGH, the Markets in Financial Instruments Directive (MiFiD) Inducement Rules attempt to reduce conflicts of interests arising out of an advising bank's double role as adviser and beneficiary of payments by the issuer. According to the MiFiD Inducement Rules, investment advisers in banks shall have the right incentive to independently advise their customers and to recommend the most appropriate product to them. This European development was the background to

5 BGH, judgment of 22 March 2016, court reference: XI ZR 425/14.

6 BGH, judgment of 21 December 2017, court reference: 1 StR 296/16.

the Fee-Based Investment Advice Act passed by the German legislator. Under the new Act, customers pay for investment advisory services and shall receive independent, tailor-made investment advice in return. While the principle of ‘decent advice for decent money’ has a long tradition in other industries, it is a departure from previous practice in the German financial industries sector.

iii Chambers for international commercial matters

Over the past years, increasing efforts have been made to enable parties in Germany to litigate court proceedings in English. As of today, courts within the districts of the Higher Regional Court of Cologne and the Higher Regional Court of Dusseldorf, as well as the Regional Court of Frankfurt/Main, allow the parties to conduct oral hearings in English, provided the parties have previously agreed thereon and the underlying case has an international dimension. However, as the pleadings as well as the judgment itself must still be in the German language, there have been discussions to establish permanent international court chambers.

In February 2018, a draft bill was submitted to the German Federal Council that would authorise state governments to establish chambers for international commercial matters, allowing the parties to conduct court proceedings completely in English. Although the draft bill contains encouraging proposals, its prospects of success must be met with scepticism: earlier legislative initiatives repeatedly found no support in Parliament.

III CHANGES TO COURT PROCEDURE

i German civil procedure principles

German civil procedure rules differ from common law civil procedure rules (particularly English common law) in several ways (e.g., in Germany there is no discovery). Furthermore, the parties are not allowed to testify as witnesses – they can only be heard in evidence in exceptional circumstances. Though the parties are responsible to present the facts to the court in both jurisdictions, the results vary. While it can only adjudicate on issues according to the claimant’s application, a German court – in contrast to English civil procedure law – is not bound by the legal assessment presented by the parties. Instead, it is free to assess the problem in any way that takes account of the facts. Also, the fee structures are different, with cost recovery rules in the event of winning the action limited to statutory fees in Germany, as opposed to the more flexible English rules.

ii Model Procedure Act

Class actions are not possible under German civil procedure law. In capital markets disputes, however, there is a possibility of filing an application for model proceedings under the Capital Investor Model Procedure Act (KapMuG). This was introduced to address inefficiencies for the claimant in such disputes.

A model procedure is initiated if one investor requests a model procedure and nine other related applications are lodged within six months (‘application proceeding’). The trial court issues an order for reference to the Higher Regional Court and defines the questions the Higher Regional Court needs to answer that are relevant to all proceedings (‘intermediate proceeding’).⁷ Following this, all trials affected by the model procedure are suspended

⁷ Section 2, subsection 1, sentence 1; Section 6, subsection 1 KapMuG.

*ex officio*⁸ ('suction effect' of the KapMuG).⁹ Once the Higher Regional Court has ruled on the posed factual and legal questions, the trial courts need to decide the individual cases ('continuation at trial level') in accordance with the Higher Regional Court's findings.¹⁰

The necessity of bringing an individual case regardless of KapMuG model proceedings is one of the major detriments to claimants. Only a few KapMuG proceedings have been conducted in over 10 years, without discernible time savings but often added complications because of the KapMuG procedure. Nevertheless, the KapMuG benefits defendants as it bundles the claims against the corporation and gives the defendants the opportunity (and necessity) of obtaining specialist single-source legal advice.

Drawing on the experience of the KapMuG, the German legislator has now introduced a 'General Model Procedure' into general civil procedure law, which takes effect in November 2018.¹¹

IV INTERIM MEASURES

See Section II.i, above, with regard to the EAPO.

i Measures under national German law: seizure and injunctions

National German law knows two legal instruments to obtain temporary relief: seizure and injunctions.

Seizure and injunctions are distinguished by the form of claim they aim to secure. While seizure is used to secure the enforcement of a monetary claim by seizing either movable or immovable property,¹² injunctions are used to safeguard non-monetary claims. The essential requirements are similar.

Seizure exists as personal seizure¹³ or seizure *in rem*.¹⁴ Seizure is possible if the enforcement of an already existing or future judgment might be obstructed or significantly encumbered. In case the seizure secures the enforcement of a future judgment, the respondent can request the court to set a deadline for initiating the main proceedings. Should the applicant fail to bring the main action within this time frame, the court may set aside the seizure order upon request.¹⁵ Personal seizure is only possible if a seizure *in rem* is not sufficient to protect the applicant (e.g., if it is unclear where the debtor holds domestic assets). Further requirement for a personal seizure is that the debtor has assets liable to attachment.¹⁶ Personal seizure can result in the arrest of the debtor.¹⁷

8 Section 8, subsection 1 KapMuG, meaning that no individual trials on the same matter are allowed to proceed.

9 New cases can join the model procedure or be registered to suspend the limitation period without being bound by the model procedure decision, Section 10, subsection 2 KapMuG.

10 Section 22 KapMuG.

11 www.bmjv.de/SharedDocs/Gesetzgebungsverfahren/Dokumente/RegE_Musterfeststellungsklage.pdf?__blob=publicationFile&v=2.

12 Section 916, subsection 1 Civil Procedure Code.

13 Section 918 Civil Procedure Code.

14 Section 917 Civil Procedure Code.

15 Section 926 Civil Procedure Code.

16 Higher Regional Court Karlsruhe, judgment of 7 May 1996, court reference: 2 UF 59/96.

17 Section 933 Civil Procedure Code.

Injunctions occur in three different types: they can (1) protect individual claims against change that might frustrate the creditor's claim; (2) temporarily regulate a legal relationship; or (3), in exceptional circumstances, directly order performance of the claim.¹⁸ All injunctions require an injunctive claim (i.e., a substantive claim) and injunctive cause (i.e., the reason for applying for injunctive relief rather than filing main proceedings), which is usually urgency. Deviating from the usual rules of evidence, *prima facie* evidence by affirmation in lieu of an oath is sufficient.

ii A practical example

A request for writ of seizure can be a dangerous tool because of the lower standard of proof and the fast pace of the proceedings. In 2016, a major German bank was subject to the attempt to seize bank assets amounting to US\$97 billion based on hundreds of pages of forged documents alleging a contractual relationship. The request was filed with the court on a Friday afternoon at 3pm. While granting the seizure request does not trigger a necessity to give reasons,¹⁹ the dismissal of the request must be accompanied by reasons to enable the applicant to appeal against it.²⁰ Against this background, the applicants might have had speculated – unsuccessfully – that on a Friday afternoon, the court would be more likely to issue the writ rather than closely study the case file and subsequently schedule an oral hearing. In the end, the applicants' lawyers withdrew the request for a writ of seizure after the defendant had pointed out that the documents produced to justify the application were forged and that no contractual relationship existed between the parties.

V LAWYER–CLIENT PRIVILEGE

Under German law, there is no formal concept of lawyer–client privilege. However, to a certain extent, client information is protected.

i Professional secrecy

German lawyers may not disclose any information they obtain while practising, including the identity of their clients.²¹ Breaches of this duty can constitute a criminal offence (e.g., disclosure of a trade secret).²²

Correspondingly, lawyers and their assistants can refuse to testify in court regarding aspects covered by their duty of professional secrecy.²³

18 Higher Regional Court Frankfurt, court order of 2 February 2004, court reference: 19 U 240/03.

19 Vollkommer in: *Zöller Commentary on the Civil Procedure Code*, 31st edition 2016, Section 922, margin No. 10.

20 Drescher in: *Munich Commentary on the Civil Procedure Code*, 5th edition 2016, Section 922, margin No. 10; Vollkommer in: *Zöller Commentary on the Civil Procedure Code*, 31st edition 2016, Section 922, margin No. 10.

21 Section 43, subsection 2 German Federal Lawyers' Act; Section 2 Professional Code for German Lawyers.

22 Section 203 German Criminal Code.

23 See, Section 53 et seq. German Criminal Procedure Code; Section 383, subsection 1, No. 6 Civil Procedure Code.

ii Seizure of documents

Documents are protected from seizure by law enforcement authorities depending on their content and location. They only cannot be seized in a criminal law context if the client is charged with a crime and the documents refer to his or her defence (e.g., communication from the defence lawyer, notes by the lawyer and notes or correspondence by the client prepared for his or her defence).²⁴ Exceptions apply if the lawyer is under investigation or if he or she holds objects that were instrumentalities.²⁵

With regard to law firms conducting internal investigations, it is much debated whether documents in an internal investigation prepared and held by external lawyers can be seized by law enforcement agencies.²⁶ While the dogmatically correct way of addressing the problem is still uncertain – especially in the absence of a clarification by the BGH – law enforcement agencies, in practice, have searched high-profile law firms and seized internal investigation documents. In March 2017, for example, Jones Day was raided in relation to the VW emissions scandal.²⁷ The question of whether or not such seizures were legitimate is currently the subject of proceedings initiated by Jones Day who filed a constitutional appeal at the Federal Constitutional Court against the seizure of documents. Although the proceedings are still pending, the court has already ordered the public prosecutor by way of an interim measure to refrain from utilising any of the documents seized until its final decision.

Still, Jones Day is not the only law firm that has been subject to on-site searches: Hengeler Mueller and Gleiss Lutz have been raided in connection with the *Deutsche Bank/Kirch* dispute,²⁸ and Freshfields Bruckhaus Deringer was compelled to hand over an internal investigation report in connection with the *HSH Nordbank* disaster.²⁹ Against this background, it is not surprising that a common strategy of claimants in banking litigation disputes is to instigate or to wait for the outcome of criminal or regulatory investigations by the authorities and then to participate using the collected evidence by inspecting the files of the authority.

VI JURISDICTION AND CONFLICTS OF LAW

Jurisdiction and conflicts of law issues do not play a significant role in German banking law disputes. Occasionally, cases occur that German courts primarily decide on the basis of procedural aspects, such as the cases *JPM v. BVG*³⁰ and *UBS v. Wasserwerke Leipzig GmbH*.³¹ In both cases, the German-resident Wasserwerke Leipzig GmbH and BVG, which both provided services for the public, suffered losses from derivatives. Because of their losses, they suspended

24 BGH, judgment of 25 February 1998, court reference: 3 StR 490/97.

25 Section 97, subsection 2, sentence 3 Criminal Procedure Code.

26 In favour of seizing documents: Regional Court Hamburg, court order of 15 October 2010, court reference: 608 Qs 18/10. Against seizing documents: Regional Court Mannheim, court order of 3 July 2012, court reference: 24 Qs 1/12, 24 Qs 2/12; Regional Court Braunschweig, court order of 21 July 2015, court reference: 6 Qs 116/15 [affirms freedom of seizure held at the corporation as preparatory measures to a defence in administrative offences trial].

27 www.nytimes.com/2017/03/16/business/volkswagen-diesel-emissions-investigation-germany.html?_r=0.

28 www.thelawyer.com/issues/online-march-2014/gleiss-lutz-and-hengeler-raided-over-deutsche-bank-lawsuit/.

29 Regional Court Hamburg, decision of 15 October 2010, court reference: 608 Qs 18/10.

30 Court of Justice of the European Union, judgment of 12 May 2011, court reference: C-144/10.

31 *UBS AG v. Wasserwerke Leipzig GmbH* [2014] EWHC 3615 (Comm).

payment under the respective derivative, which prompted their contractual counterparties to bring a claim before the High Court of Justice in London. In turn, both Wasserwerke Leipzig and BVG brought an action before German courts, seeking damages and claiming that the derivative was invalid as they had acted *ultra vires*. Wasserwerke Leipzig GmbH and BVG argued that, as they had acted *ultra vires*, the German courts enjoyed exclusive jurisdiction under Article 22(2) of the Brussels I Regulation. In a preliminary ruling, the Court of Justice of the European Union denied the applicability of Article 22(2) of the Brussels I Regulation, which led to the lawsuits in Germany being inadmissible.³²

VII SOURCES OF LITIGATION

Banking litigation typically arises from claims of mis-selling, prospectus liability or mistrades. However, recently there has been a significant increase in litigation against the decisions of the regulator and discussions in academia regarding banks' liability in the context of the manipulation of reference indexes.

i Mis-selling

According to the *Bond* decision,³³ an investment advice contract is concluded by way of implicit conduct whenever information about a financial product is given and the (potential) investor noticeably relies on this information. In principle, this even applies to situations in which the standard terms and conditions used exclude the conclusion of an investment advice contract without prior written consent.³⁴

To comply with legal requirements, investment advice needs to be tailored to the customer and to the product,³⁵ taking into account the personal circumstances of the customer, the customer's risk appetite, envisaged investment period and personal experience with financial products in general and products of this kind, etc. Although the level and extent of appropriate advice differ in each individual case, a good rule of thumb states that the less experienced the customer and the more complex the suggested product is, the higher the extent and level of advice necessary.

Against this background, it is not surprising that mis-selling cases have become common with regard to retail clients – for instance, in form of the series of kickback decisions by the BGH – and also in respect of institutional clients if an investment product failed.

32 Court of Justice of the European Union, judgment of 12 May 2011, court reference: C-144/10.

33 BGH, judgment of 6 July 1993, court reference: XI ZR 12/93.

34 Petra Buck-Heeb, ZIP 2013, pp. 1401-1411; Schmitt in: Zerey (ed.) *Financial Derivatives*, fourth edition 2016, p. 827.

35 BGH, judgment of 29 April 2014, court reference: XI ZR 130/13.

ii Prospectus liability

As in other countries, prospectus liability claims have been a classic banking litigation theme in Germany as well. German law differentiates between several different types of prospectus liability regimes depending on the product in question.³⁶ However, it is common for all types of prospectus liability that it constitutes a liability not to inform the (potential) investor about facts that are essential to drawing one's own conclusions in respect of the chances and risks attached to the investment.³⁷

iii Mistrades

Regarding mistrades, Germany has a whole industry of so-called mistrade hunters – often former traders who lost their jobs in the course of the financial crisis – who look for false prices and try to exploit these situations. Such mistrade hunters often use specialised technology to detect wrong pricing. They know about the limits of the bank that trigger manual double-checking of the appropriateness of the trade. To avoid these checks, they adapt their trading quantity accordingly by splitting trades. After a cancellation or avoidance of such a mistrade, the mistrade hunters allege having acted in *bona fides*. They claim that the mistrade rules allowing such avoidance are void, and that the statutory avoidance regime does not apply to their case, etc. Usually, such mistrade hunters seek an amicable out-of-court settlement.

iv More proceedings against the supervisory authority

Whereas in the past, there were practically no court proceedings between financial institutions and their supervisory authorities, there has been a significant increase in such court proceedings given the tighter regulation, the authorities' more aggressive behaviour and the overall more competitive environment for banks. One prominent example of this is the dispute between L Bank and the European Central Bank (ECB) concerning the appropriateness of direct supervision of the ECB, which incurs additional costs to the bank.³⁸

v Impact of the manipulation of reference indexes

There is currently a debate in legal literature as to whether banks that were involved in the manipulation of reference indexes, such as LIBOR, can be held responsible. Three factors are being debated: (1) the calculation of the damage as the 'fair' reference index is hardly determinable; (2) the causal link between the specific act and the damage since the highest and the lowest bid are excluded; and (3) the (standard of) fault (at least in cases where the bank's management did not know about the manipulation).

36 For products in form of a security: German Securities Prospectus Act; for all fund investments: Section 306 German Capital Investment Code; and for all other products: Sections 20 et seq. German Capital Investment Act. This prospectus liability regime is completed by the civil-law prospectus liability in the strict sense, which nowadays has been superseded in the vast majority of cases, BGH, court order of 21 October 2014, court reference XI ZB 12/12, paragraphs 64 et seq.

37 BGH, judgment of 31 May 1990, court reference: VII ZR 340/88.

38 The L Bank lost the action, cf. European General Court, judgment of 16 May 2017, court reference: T-122/15.

vi Further trends to be noted

It can be assumed that German civil courts will increasingly have to deal with cases regarding cum-ex transactions. Cum-ex trades involve the acquisition of shares with (cum) dividends due on or just before the dividend record date and delivery of these shares after the dividend record date without (ex) dividends. These transactions typically led to a double credit or refund of dividend withholding tax that was only paid to the German tax authorities once. In January 2012, the German legislator closed the gap in the law that made such multiple credits or refunds possible.

So far, two German court proceedings have become public in which investors in products whose performance relied on making use of cum-ex trades managed to successfully claim more than €48 million in damages against their advising banks; the courts found that the bank failed to properly explain the underlying tax concept and risks.³⁹ In addition, even custodian banks that only executed said trades may also be subject to claims. For instance, investors who were not aware that their investment or trade was part of a cum-ex deal may decide to pursue claims for losses suffered by tax clawbacks.

VIII EXCLUSION OF LIABILITY

Under German law, it is extremely difficult to effectively exclude liability. Usually, only a balanced reduction of liability is possible. The least strict regime applies to individual agreements. Individually negotiated exclusions of liability must only comply with public policy (*contra bonos mores*).⁴⁰ However, most exclusions of liability will be part of standard terms and conditions.⁴¹ In these, an exclusion of liability for the main duties under a contract is usually not possible if the exclusion threatens to thwart the objectives of the contract.⁴² It is generally impossible to limit one's own liability for grossly negligent or intentional behaviour in standard terms and conditions in relation to consumers. The same applies with regard to entrepreneurs if the contractual counterparty is unreasonably disadvantaged by it (Section 307 Civil Code). A 'surprising clause', such as one concerning the investment broker's liability in a fund joining agreement, does not become part of the contract (Section 305c Civil Code).⁴³

Furthermore, the exclusion of liability must not infringe the principles of *bona fides*. For instance, a clause excluding the conclusion of an investment advice contract while effectively providing investment advice constitutes a *venire contra factum proprium* and renders the clause inapplicable.⁴⁴

39 Regional Court Munich I, court reference: 34 O 680/16 (unpublished); Regional Court Ulm, judgment of 22 May 2017, court reference: 4 O 66/33.

40 Section 138, subsection 1 Civil Code.

41 Sections 305 et seq. Civil Code.

42 BGH, judgment of 14 November 2000, court reference: X ZR 211/98.

43 BGH, judgment of 11 December 2003, court reference: III ZR 118/03.

44 Petra Buck-Heeb, ZIP 2013, pp. 1401-1411; Schmitt in: Zerey (ed.) *Financial Derivatives*, fourth edition 2016, p. 827.

IX REGULATORY IMPACT

One result of the crisis has been a marked increase of financial regulation. Alongside the implementation of the European Banking Authority, the MiFID reform and the implementation of the Basel III framework (CRD IV), several new regulatory mechanisms have been introduced (single supervisory and single resolution mechanisms). These all lead to a higher standard of supervision. The emphasis of these new pieces of regulation lies on early intervention.

Under the new regulatory framework, regulators intervene earlier and – as a further lesson learned from the financial crisis – more aggressively. Often, regulators expect an internal investigation of possible regulatory breaches – and threaten to sanction non-compliance with a special audit pursuant to Section 44a of the German Banking Act, which is a particularly expensive tool to investigate a potential issue. Furthermore, regulators place a high emphasis on international coordination. Such increased cooperation by authorities means that regulatory and criminal investigations can overlap.

Banks, on the other hand, are pressured by the increased scrutiny. In some instances, banks have even brought proceedings against their regulators themselves (e.g., L Bank (see Section VII.iv, above)). This shows a drastic shift in culture by banks. Previously, it was deemed prudent not to challenge the regulator but instead to let regulatory authorities proceed with their work. In light of more aggressive regulators, banks increasingly decide on a more confrontational approach. This results in a more litigious environment.

X LOOKING AHEAD: NO DOWNTURN EXPECTED

In recent years, there have been several developments in the banking law sector. One is a strong increase in private investor cases brought to state courts in the wake of the financial crisis. This is helped by widespread legal cost insurance, which makes it less of a risk for private investors to bring an action. Even though German courts have a reputation for being investor-friendly, banks usually prefer litigation in front of state courts to alternative dispute resolution mechanisms. That said, the speed of court proceedings has varied depending on the capacity that the individual courts can free up to manage the rise of investor-brought cases in recent years.

Another development is that banks are more willing to litigate against institutional clients than in the past. This corresponds with legislative pressure on banks and an increasingly competitive environment for financial institutions – especially in a market like the German market, which is considered to be overbanked. Furthermore, in the past three years, more professional process funders have entered the German market,⁴⁵ which also fosters the trend of more litigation. Given the new aggressive stance adopted by regulators, their international cooperation and law enforcement authorities' latest focus on banking-related criminal investigations on the one hand, and banks' determination to take their regulators to court on the other, there is no expectation that the number of banking litigation cases in Germany will drop.

⁴⁵ E.g., for claims against Volkswagen, as well as cases concerning JuraXX or Sportgate AG.

HONG KONG

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I SIGNIFICANT RECENT CASES

Many of the more notable cases involving banks have concerned allegations of mis-selling of financial products by private and retail banks that have worked their way through the courts since the 2008 global financial crisis and have, by and large, now been resolved. The cases have typically addressed the scope of the banks' duties and the effectiveness of disclaimers in client agreements, often finding in favour of the banks on the basis of their client agreements. In response to these cases, from June 2017, the Securities and Futures Commission (SFC) introduced a mandatory clause in client agreements to make suitability a contractual obligation and prevent any derogation from it. Sections VII and VIII, below, address these cases, while Section IX addresses the SFC's reaction in its mandatory suitability clause.

In mis-selling cases and many other areas of litigation that affect banks, English cases continue to be persuasive authority in Hong Kong, particularly those of the Privy Council and Supreme Court. To the extent that the English Courts are deciding cases that affect banks, including all the recent contract cases, these will continue to be relevant to banks operating in Hong Kong.

In some areas, Hong Kong law has not followed English law on questions of law that affect banks. For instance, Hong Kong contract law on penalty clauses has not kept up with English law developments. In a 2016 decision, the Hong Kong Court of Appeal upheld a liquidated damages clause on the basis that it was a 'genuine pre-estimate of loss'.² In doing so it upheld the century-old *Dunlop* test on penalties that was overruled by the Supreme Court in England and Wales in *Cavendish* in its 're-explanation' of the law on penalties by reference to unconscionability (it was decided between the hearing and handing down of the judgment in *Brio* by the Hong Kong Court of Appeal).³ Despite this divergence, the Court of Appeal did indicate its support for a broader, commercial approach, which banks entering into commercial contracts in Hong Kong should bear in mind.

II RECENT LEGISLATIVE DEVELOPMENTS

Third-party rights are a frequent consideration in practice for banks. The Contracts (Rights of Third Parties) Ordinance reformed the doctrine of privity of contract when it came into effect in January 2016. The Ordinance brought Hong Kong law into line with the approach to

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2 *Brio Electronic Commerce Limited v. Tradelink Electronic Commerce Limited* [2016] 2 HKLRD 1449.

3 *Cavendish Square Holding VB v. Talal El Makadesi; ParkingEye Limited v. Beavis* [2015] UKSC 67.

privity in many overseas jurisdictions, such as England and Wales, Singapore and New York. In doing so, it allows parties the flexibility to confer rights on third parties in their contracts, and if so, on what terms those third parties should receive those rights. These rights can be enforced by third parties, subject to certain exceptions including bills of exchange, promissory notes and letters of credit. Once the third party has an enforceable right, the original parties may not alter or remove the right without the third party's consent. The Ordinance sets out a two-limb test, under which a third party may enforce a term of a contract (including a term that excludes or limits liability) if:

- a* the contract expressly provides that the third party may do so; or
- b* the term purports to confer a benefit on the third party, unless on a proper construction of the contract, the term is not intended to be enforceable by the third party. There is therefore a presumption in this case in favour of the third parties having rights.

Parties to a contract can expressly exclude the application of the Ordinance in their contracts. To minimise the potential scope for litigation about whether a term falls within the second limb, parties will often consider either expressly conferring rights under the Ordinance, or expressly excluding its operation. Given that the law on third party rights is new to Hong Kong, market practice as between banking, corporate, and debt and equity capital markets transactions still tends to differ in the approach to the application of the Ordinance, particularly relating to indemnities for third parties.

Competition law has occasionally been an area of interest for banks in light of the global LIBOR and FX investigations. With the Competition Ordinance that came into force in December 2015, after many years in the making, Hong Kong enacted its first economy-wide competition law. The law prohibits anticompetitive agreements and abuses of substantial market power and brought Hong Kong in line with many developed jurisdictions in the world. In 2015, the Competition Commission published its enforcement and leniency policies and the Competition Tribunal, responsible for adjudicating cases brought by the Commission, established its rules of procedure. The Commission commenced its first two cases in 2017, both of which are set for trial this year. These cases, which concern alleged tender rigging in the IT industry and alleged cartel activity in the construction and engineering sector, will give the Tribunal the opportunity to clarify points of law that are unclear under the Competition Ordinance. The Commission is also expected to revise its enforcement and leniency policies in 2018 and reinvigorate its law enforcement approach with a stronger focus on cartel activity, bolstered by a new budget of HK\$200 million granted by the government and new senior management with litigation experience and a background in cartel enforcement. Applications to the Commission for leniency, for decisions on exclusion or exemption or for block exemption orders, are likely to remain a rarity, with only one application for a block exemption order having been made since the enactment of the Competition Ordinance.

The Financial Institutions (Resolution) Ordinance and the Financial Institutions (Resolution) (Protected Arrangements) Regulation came into operation in July 2017.⁴ The Ordinance establishes a regime for the orderly resolution of financial institutions in the banking sector and systemically important financial institutions in the insurance and securities and futures sectors, as well as certain financial market infrastructures in Hong

⁴ Except Part 8, Section 192 and Division 10 of Part 15.

Kong. In addition, the resolution regime seeks to provide the relevant resolution authorities with administrative powers in order to mitigate the risks posed by the non-viability of an in-scope institution to the stability and effective working of Hong Kong's financial system.

Finally, the Apology Ordinance was passed by the Legislative Council in July 2017 and came into force on 1 December 2017. The Ordinance is intended to promote and encourage the making of apologies with a view to facilitating the amicable resolution of disputes. The Ordinance defines an apology broadly, covering expressions of regret, sympathy or benevolence, including an admission of fault or liability. The expression may be oral, written or by conduct. Apologies made on or after the commencement of the Apology Ordinance are deemed inadmissible in determining fault or liability, save in limited circumstances, such as in criminal proceedings. Apologies are also deemed not to void or otherwise affect insurance cover. The Apology Ordinance brings Hong Kong law in line with many other common law jurisdictions and is a welcome development in facilitating the amicable resolution of disputes.

III CHANGES TO COURT PROCEDURE

Since the Civil Justice Reforms (CJR) were implemented in 2009, modelled in large part on the Civil Procedure Rules introduced by the Woolf reforms in England and Wales in 1999, there has been little material change to court procedure. The objectives of the CJR included promoting greater use of active case management, streamlining civil procedures, expediting the hearing of cases and facilitating early settlement. A committee established by the Chief Justice has continued to monitor the workings of the justice system and make suggestions to the Chief Justice to ensure its smooth operation. When its last report was published in 2017, the average number of days from commencement of an action to trial had followed a rising trend over a cumulative six-year basis.

In 2014, the Commercial List of the High Court introduced a pilot scheme practice direction for electronically stored documents for 'reasonable, proportionate and economical discovery' that introduced the concept of reasonable search by reference to a range of factors, including the number of electronic documents, the complexity of proceedings, the ease of retrieval and significance of the documents.⁵ It contemplates the use of keyword searches, staged production and the use of 'technology-assisted review' by concept searching and data sampling, paving the way for the use of predictive coding technologies. While the practice direction is intended for use in the Commercial List, parties can apply it by agreement, or at the direction of the court.⁶

Group litigation orders and multiparty litigation are yet to feature in Hong Kong and are unlikely to affect banks in the near future. The Law Reform Commission of Hong Kong (LRC) published a report in 2012 proposing that a mechanism for class actions be adopted in Hong Kong, starting with consumer cases (tort and contract claims by consumers in relation to goods, services and property). A working group on class actions chaired by the Solicitor General and comprised of representatives of the legal profession, business sectors and government officials was established in 2013 by the Department of Justice to consider the proposals of the LRC and make recommendations to the government. The working group

⁵ Practice Direction SL 1.2.

⁶ *Chinacast Education Corp & Ors v. Chan Tze Ngan* [2014] 5 HKC 277, applying the practice direction before it was implemented.

has held over 20 meetings but is still considering the LRC's recommendations and has not, at the time of publication, drafted a legislative bill for the Hong Kong Legislative Council's consideration. We await further developments in this area.

Third-party funding for litigation remains impermissible in Hong Kong with some limited exceptions, including insolvency proceedings, where liquidators continue to be active in litigation. However, in October 2016, the LRC released its final report, which recommended that the law should be amended to clearly permit third-party funding of arbitration and associated proceedings under the Arbitration Ordinance, with appropriate financial and ethical safeguards in place. The report recommended that the Arbitration Ordinance be amended to disapply the common law principles of maintenance and champerty to third-party funding. It further recommended that consideration be given to disapplying these principles to mediation under the Mediation Ordinance. The Commission felt that permitting such funding was necessary to prevent parties opting for other international arbitration seats and preserve Hong Kong's standing as a centre of international arbitration. Subsequently, the Arbitration and Mediation Legislation (Third Party Funding) (Amendment Bill) 2016 was passed by the Legislative Council in June 2017, adding a new Part 10A to the Arbitration Ordinance and a new Section 7A to the Mediation Ordinance, to disapply maintenance and champerty to third-party funding in arbitration and mediation (subject to ethical and financial safeguards). The legislation brings Hong Kong in line with England and Wales, Australia and Singapore, among others.

The ever growing cross-border business for banks between Hong Kong and China has increased the importance of the collection of evidence for litigation between them. In March 2017, the Arrangement on Mutual Taking of Evidence in Civil and Commercial Matters between the Courts of the Mainland and Hong Kong (the Arrangement) came into force to close the gap caused by the inapplicability of the Hague Evidence Convention between Hong Kong and the mainland as parts of the same country. Under the Arrangement, parties can make letter-of-request applications for evidence through the designated liaison authorities in the Chinese language. The scope of assistance that may be requested by a Hong Kong court and a mainland court differ. While mainland courts can request the Hong Kong courts to examine witnesses, obtain documents, inspect, photograph, preserve, take into custody or detain property, take samples of property and carry out medical examination of a person, the Hong Kong courts can request the mainland courts to obtain statements from parties and testimony from witnesses, provide documentary evidence, real evidence, audiovisual information and electronic data, and conduct site examination and authentication.

IV INTERIM MEASURES

Of relevance to banks considering cross-border enforcement, the CJR introduced a regime to extend the ability of the courts to grant free-standing interim injunctive relief in support of foreign proceedings, closing a gap left by the Privy Council in 1996.⁷ Hence, under Section 21M of the High Court Ordinance, the Hong Kong court may grant an injunction or other interim relief in aid of proceedings commenced or to be commenced overseas.

In a 2016 case, the Court of Final Appeal clarified the tests to be satisfied in determining an application under Section 21M, where the plaintiff sought to freeze assets in Hong Kong in aid of a judgment in England for breach of exclusive jurisdiction clauses. The Court of

⁷ *Mercedes Benz AG v. Leiduck* [1996] AC 284.

Final Appeal held there was no breach of comity in granting a freezing injunction to protect a foreign claim for breach of an exclusive jurisdiction clause.⁸ In reinstating a freezing injunction granted in support of proceedings in the English court for breach of exclusive jurisdiction clauses, the Court of Final Appeal held that the Court of Appeal had erred in holding that it was necessary to consider whether the plaintiff had a good arguable case in its substantive proceedings under Hong Kong law. Rather, the correct test should be to consider whether the plaintiff has a good arguable case before the foreign court. The Court of Final Appeal also held that there was no bar on the ground of breach of comity, or public policy, to the grant of a freezing injunction to assist in enforcing an award (or potential award) of damages by the English court for breach of an exclusive jurisdiction clause, as the Hong Kong court was not asked to enforce the jurisdiction clause itself, in favour of the English court. This was the case even though the substantive proceedings were conducted before the Hong Kong and English courts in parallel, with conflicting judgments as to jurisdiction.

In another case concerning freezing injunctions, in November 2017, the Court of First Instance held that a bank put on notice of a freezing injunction issued over the assets of one of its account holders does not owe a duty of care to the holder of that injunction.⁹ The court applied the reasoning of the House of Lords decision in *Customs and Excise Commissioners v. Barclays Bank plc*.¹⁰ Master KC Chan held that the bank had not voluntarily assumed a duty of care to the holder of the injunction by having been served the injunction, with no other act or communication between them; the only duty arising out of the injunction was to the court and that the recognition of a duty of care in such circumstances would not be fair, just or reasonable. A bank put on notice of a freezing injunction still risks punishment for contempt of court if it breaches its duty to the court to comply with the injunction, particularly if it enables an account holder to breach the terms of the injunction. However, this case offers welcome reassurance to banks as regards their obligations to third parties in dealing with freezing injunctions against their clients.

In the field of cross-border enforcement for banks, a decision by the Court of Appeal in 2016 demonstrated the need to act promptly when seeking an anti-suit injunction in relation to proceedings commenced in a foreign court in breach of an agreement to arbitrate.¹¹ The Court of Appeal drew a distinction between *forum non conveniens*, anti-suit injunctions and contractual anti-suit injunctions, and held that the lower court did not exercise its discretion erroneously by refusing to grant anti-suit relief on the basis of the plaintiff's deliberate, inordinate and culpable delay. Delay in seeking injunctive relief, therefore, may result in the substantive claim being resolved in foreign courts, in breach of the parties' arbitration agreement.

V LAWYER–CLIENT PRIVILEGE

The Hong Kong courts have not been testing the application of privilege to internal investigations to the same extent as has been the case in England in recent years, where the

8 *Compania Sud Americana de Vapores SA v. Hin-Pro International Logistics Limited* (2016) 19 HKCFAR 586.

9 *Grasberg Capital Asia Limited v. Bank of Communications Limited* [2017] 6 HKC 256.

10 [2007] 1 AC 181.

11 *Sea Powerful II Special Maritime Enterprises (ENE) v. Bank of China Ltd* [2016] 3 HKLRD 352, upholding the Court of First Instance decision ([2016] 1 HKLRD 1032).

courts have adopted a restrictive view of the availability of legal professional privilege and litigation privilege in the context of various aspects of internal investigations that may be relevant to banks.

While the Hong Kong courts will typically have regard to English law on the availability of privilege, the Court of Appeal has widened the scope of legal advice privilege by deciding in favour of a broader definition of ‘client’ after full consideration of the relevant English law. In a welcome judgment delivered in June 2015, the Court of Appeal took the opportunity to consider and reject the narrow definition of ‘client’ for the purposes of legal advice privilege as laid down by the English Court of Appeal in the *Three Rivers (No. 5)* case.¹² Instead, the Court opted for a more liberal approach, which defines a ‘client’ as simply a corporation and its employees who could be regarded as being authorised to act for the corporation in the process of obtaining legal advice, not being limited to ‘a small group of employees within the legal department of a corporation’. Otherwise, it held that the adoption of a restrictive definition of who constitutes the client would impinge on the ability of corporations to seek and obtain legal advice, as it, ‘might well discourage those defined as the client for the purposes of legal professional privilege from seeking the input or assistance of other employees who might be better qualified or able to provide it’. A claim of legal advice privilege may therefore be made over a wider range of communications between a bank and its legal advisers.

As part of its ruling on the ambit of legal advice privilege, the Court of Appeal held that Hong Kong should adopt the ‘dominant purpose’ test as expounded by Tomlinson J in *Three Rivers (No. 5)* in setting the proper limit for legal advice privilege (i.e., if a document comes into existence as part of the continuum of communications between a lawyer and a client with a dominant purpose of getting legal advice, it should be protected by legal advice privilege). In doing so, the Court of Appeal held that there needed to be a meaningful protection of confidentiality in the process of obtaining legal advice in both the litigious and non-litigious context. The Court of Appeal considered that the dominant purpose test is capable of effectively screening out unmeritorious claims for legal professional privilege. In making its ruling on the application of the dominant purpose test, the Court noted that legal professional privilege is constitutionally entrenched in Hong Kong as a basic right under Article 35 of the Basic Law.

The Court of Appeal decision in *Citic Pacific* concerned the availability of a claim for privilege over documents seized on the execution of a search warrant, including documents where there had been a partial waiver of privilege by their production to the SFC without an express assertion of limited waiver. At first instance, the Court had in this context recognised the concept of limited waiver of privilege.¹³

Separately, the Court of Appeal confirmed in November 2015 that legal advice privilege does not extend to advice by non-lawyers (e.g., accountants advising on tax law).¹⁴ In doing so, it adopted the reasoning of the majority in the UK Supreme Court.¹⁵ Although not part of its formal decision, the Court of Appeal noted that privilege, while a substantive and fundamental right under Article 35 of the Basic Law, originates in the public interest and is

12 *Citic Pacific Limited v. Secretary for Justice* (No. 2) [2015] 4 HKLRD 20.

13 [2012] 2 HKLRD 701.

14 *Super Worth International Ltd & Ors v. Commissioner of the ICAC & Secretary for Justice* [2016] 1 HKLRD 281.

15 *R (on the application of Prudential plc and another) v. Special Commissioner of Income Tax and anor* [2013] UKSC 1.

a facet of the rule of law, which in Hong Kong means that the law of the forum is applied to determine the applicability of privilege to a document or communication (although the Court of Appeal did note that there was some room for flexibility in appropriate cases).

VI JURISDICTION AND CONFLICTS OF LAW

For the purposes of banks' consideration of whether to include state immunity waivers in their contracts, it is noteworthy that the Court of Final Appeal has ruled that absolute immunity from suit applies in Hong Kong, rather than a restrictive immunity that allows exceptions for commercial transactions. China's policy on state immunity is that of absolute immunity. By a three-to-two majority, the Court of Final Appeal held that Hong Kong cannot, as a matter of legal and constitutional principle, adhere to a doctrine of state immunity that differs from that adopted by China. The Court concluded that states also enjoy absolute immunity in the Hong Kong courts.¹⁶ Controversially, as part of its decision, the Court of Final Appeal referred the interpretation of provisions of Hong Kong's constitution in its Basic Law concerning responsibility for foreign affairs to the Standing Committee of the National People's Congress (SNPC) in Beijing for interpretation. The SNPC's interpretation was that the Hong Kong courts must give effect to the doctrine of absolute immunity as promulgated by the Central People's Government of China.

In a separate case, the Hong Kong court held that the Chinese government enjoys crown immunity in Hong Kong.¹⁷ Hence, in Hong Kong, if a state-owned entity is controlled by the Chinese government, it will also enjoy crown immunity.

The result of the two cases is that sovereign states and the Chinese government both enjoy absolute immunity from suit in Hong Kong. As absolute state immunity can only be waived 'in the face of the court' and cannot be waived in pre-dispute contractual documents, any contractual waiver or arbitration clause will not be recognised by the Hong Kong court as an effective waiver of immunity. On the other hand, active participation in the proceedings with knowledge of the right to claim immunity would be sufficient to amount to a waiver.

Of critical importance to the application of crown immunity in Hong Kong is the extent of control over the relevant entity by the Central People's Government. In a 2017 decision, the court held that a Chinese state-owned entity could not invoke crown immunity when it was undertaking commercial activities and did not satisfy the test of being an entity controlled by the Chinese government, unlike the position of the entity concerned in the *Intraline* case.¹⁸

Separately, the Department of Justice released a consultation paper on the 2016 Preliminary Draft Convention on the Recognition and Enforcement of Foreign Judgments, modelled on and complementing the 2005 Hague Convention on Choice of Court Agreements. The Draft Convention sets out the criteria for the courts of one Member State to recognise and enforce judgments in civil and commercial matters rendered by the courts of other Member States. If widely accepted across different jurisdictions, and if Hong Kong becomes a signatory, it would provide judgment creditors with a potentially more popular mechanism for enforcing their judgments outside of Hong Kong, and a regime for judgment creditors to enforce foreign judgments in Hong Kong that do not currently qualify for enforcement under the Foreign Judgments (Reciprocal Enforcement) Ordinance (which

16 *FG Hemisphere Associates LLC v. Democratic Republic of the Congo & Ors* (2011) 14 HKCFAR 95.

17 *Intraline Resources Sdn Bhd v. The Owners of the Ship or Vessel 'Hua Tian Long'* [2010] 3 HKLRD 611.

18 *TNB Fuel Services Sdn Bhd v. China National Coal Group Corporation* [2017] HKEC 1184.

currently applies to the judgments of 15 countries: Australia, Austria, Belgium, Bermuda, Brunei, France, Germany, India, Israel, Italy, Malaysia, the Netherlands, New Zealand, Singapore and Sri Lanka – but not the United Kingdom), and China under the Mainland Judgments (Reciprocal Enforcement) Ordinance.

VII SOURCES OF LITIGATION

Mis-selling claims concerning financial products sold by private and retail banks have been the most notable feature of liability for banks in Hong Kong since the 2008 global financial crisis, although the cases have mostly been resolved. These claims typically raise issues relating to the nature and scope of the duty owed by the bank to its customer, liability for misrepresentation, the ability of claimants to import regulatory suitability provisions from the SFC's Code of Conduct as implied duties in contract or tort, and contractual disclaimers.

In the main, the courts have found in favour of the banks, often because of the strict interpretation of their contractual terms and conditions that allocate the parties' risks and responsibilities, narrowing the scope of duty or disclaiming responsibility (or both). These decisions have typically not allowed express contractual terms to be interpreted differently through implied terms, introduction of regulatory provisions or tortious duties not otherwise stated in the contract. The courts have given short shrift to various attempts to imply contractual or tortious duties into the clear language of client agreements based on the provisions of the SFC's suitability requirements in its Code of Conduct.

Against more sophisticated individual clients, banks have mostly been successful in relying on the express terms of their client agreements to assert that the account was 'execution only'. Hence the bank has no duty to advise the client or manage the account, and even if any advice was given the customer was not entitled to rely upon it, regardless of whether the client fully read or understood the client agreements.¹⁹ Generally, the courts have been unwilling to find an advisory duty where none was agreed.

Claimants ran misrepresentation claims based on a mixture of common law, the Misrepresentation Ordinance and Section 108 of the Securities and Futures Ordinance (a statutory framework for reckless, negligent and fraudulent misrepresentation claims). Although many of the investment products involved were often complex structured products with asymmetrical risk profiles, many of them being forward accumulators,²⁰ forensic review of the communications often revealed conduct consistent with the written terms in client agreements and not supportive of the pleaded misrepresentation theories. Even if the banks had made misrepresentations and departed from an 'execution-only' role, the express terms of client agreements contractually estopped claimants from claiming reliance on any alleged misrepresentations or imposing an advisory duty onto the bank following the *Springwell*²¹ line of authority.²²

19 *Kwok Wai Hing Selina v. HSBC Private Bank (Suisse) SA* [2012] 4 HKC 260; *DBS Bank (Hong Kong Limited) v. San-Hot HK Industrial Company Limited and Hao Ting* [2013] HKEC 352; *DBS Bank (Hong Kong) Ltd v. Sit Pan Jit* [2015] HKEC 548, [2016] HKEC 1307.

20 Known in the local market colloquially as 'I'll kill you later's'.

21 *JPMorgan Chase Bank & Ors v. Springwell Navigation Corp* [2010] EWCA Civ 1221, which held that the principle of contractual estoppel will uphold the bank's terms and conditions to prevent allegations of misrepresentation or setting up of an advisory duty.

22 *DBS Bank (Hong Kong Limited) v. San-Hot HK Industrial Company Limited and Hao Ting* (see footnote 19, above); *DBS Bank (Hong Kong) Ltd v. Sit Pan Jit* (see footnote 19, above).

However, in two more recent cases, the court has ruled that the banks could not rely on express contractual restrictions to avoid liability. In *Chang Pui Yin*, the Court of Appeal found for the investors in holding that standard non-reliance clauses contravened the Unconscionable Contracts Ordinance, and failed to meet the reasonableness requirements under the Control of Exemption Clauses Ordinance (CECO), departing from the decision in *San-Hot* on the facts, where similar non-reliance clauses were held to define the scope of the bank's relationship with its client.²³ In *Li Kwok*, the Court of First Instance also found that the bank could not rely on its standard risk disclaimers to exclude liability as they failed to meet the reasonableness requirements of the CECO, distinguishing from *San-Hot* and *Springwell* on the facts as the relevant investments in *Li Kwok* were purportedly low risk.²⁴

VIII EXCLUSION OF LIABILITY

Perhaps unsurprisingly, the banks have generally been successful in relying on the principle of contractual estoppel by pointing to the risk disclaimers often found in account agreements. The language of these risk disclaimers would usually contain clauses confirming that no advisory duty is owed, the client places no reliance on the bank, and that his or her investment decisions were his or her own and that he or she accepted and understood the risks attached. Even if misrepresentations had been made by the bank's representatives to the client regarding the essential features of the financial product involved, the principle of contractual estoppel prevents clients from successfully asserting that he or she relied on any representations made, and that he or she made independent decisions in deciding to invest, and accepted and understood the risks attached to the investment.

In some cases, the Court of First Instance and the Court of Appeal have also held²⁵ that a bank may rely on the risk disclaimers in standard terms in signed contracts, despite the terms not being specifically drawn to the client's attention. In reaching this conclusion, the Courts have highlighted the English case *Interfoto*²⁶ on onerous clauses, which held that reasonable notice of the relevant terms must be given to a contracting party for them to be effective.²⁷

In these mis-selling claims the courts have generally followed *Springwell*²⁸ in upholding the express contractual terms as the basis for determining the rights and obligations between the client and the bank. Under the Control of Exemption Clauses Ordinance, exemption clauses are subject to the test of reasonableness. The relevant line of authorities²⁹ also determined that a clause can only be categorised as an exemption or exclusion clause if it has the effect of limiting liability for obligations that have been expressly promised or offered. However, standard terms setting out the role of the bank and the scope of the services the

23 *Chang Pui Yin v. Bank of Singapore Ltd* [2017] HKEC 1493.

24 *Li Kwok Heem John v. Standard Chartered International (USA) Ltd* [2016] HKEC 7.

25 *DBS Bank (Hong Kong Limited) v. San-Hot HK Industrial Company Limited and Hao Ting* (see footnote 19, above); *DBS Bank (Hong Kong) Ltd v. Sit Pan Jit* (see footnote 19, above).

26 *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* [1989] 1 QB 433.

27 *DBS Bank (Hong Kong Limited) v. San-Hot HK Industrial Company Limited and Hao Ting* [2013] (see footnote 19, above); *DBS Bank (Hong Kong) Ltd v. Sit Pan Jit* (see footnote 19, above).

28 *JPMorgan Chase Bank v. Springwell Navigation* (see footnote 21, above).

29 *Kwok Wai Hing Selina v. HSBC Private Bank (Suisse) SA* (see footnote 19, above); *DBS Bank (Hong Kong Limited) v. San-Hot HK Industrial Company Limited and Hao Ting* (see footnote 19, above); *DBS Bank (Hong Kong) Ltd v. Sit Pan Jit* (see footnote 19, above).

bank contracted to provide were not exclusion clauses at all, despite language such as ‘the bank assumes no responsibility’ or ‘the bank shall have no liability’, because they typically prescribe the scope of the duty, rather than seek to exclude it.

The various contractual terms defining the nature and scope of the services that the bank contracted to provide were also held not to be exclusion clauses that would be subject to the Control of Exemption Clauses Ordinance in *San-Hot*.³⁰ In another case, a client was introduced to a Madoff fund by the bank.³¹ The court held that the misrepresentation claim was made out, the contractual estoppel defence failed and the bank’s risk disclosure statement failed to satisfy the requirement of reasonableness under the Control of Exemption Clauses Ordinance. However, the court held that the bank could not have reasonably detected the fraud and therefore the client’s case failed.

On the other hand, in an exceptional case where the courts found against the bank, the relevant contractual terms were unclear, resulting in the bank being held to have breached its contractual duty to advise in a case where the clients were an elderly couple with modest backgrounds and little understanding of investment products.³² Once the bank’s advisory role had been established, and in the absence of an express scope of the bank’s duty to provide advice, the court held that there was an implied duty to exercise reasonable care and skill in the performance of that advisory role. This meant that the adviser had to exercise reasonable care and skill with regard to the investors’ investment objectives and risk appetite, must offer products that are suitable to those investment objectives and risk appetite, and warn the investors of the risks inherent in the investment. The court held that the bank failed to do so in that case, and went on to say that if it was wrong and the banking relationship between the parties was actually ‘execution only’ then the bank would have succeeded in its defence of contractual estoppel based on the contractual documentation.

IX REGULATORY IMPACT

In response to the courts’ decisions upholding disclaimers in client agreements in favour of banks, the refusal to imply duties into client relationships based on suitability requirements in its Code of Conduct and the contractual estoppel defence, the SFC has made professional investor and client agreement requirements more stringent. From June 2017, under the revised SFC Code of Conduct, all client agreements are required to incorporate the new ‘no derogation’ clause:

If we [the intermediary] solicit the sale of or recommend any financial product to you [the client], the financial product must be reasonably suitable for you having regard to your financial situation, investment experience and investment objectives. No other provision of this agreement or any other document we may ask you to sign and no statement we may ask you to make derogates from this clause.

Further, the inclusion of clauses that are inconsistent with the Code of Conduct, or that misdescribe the actual services provided to clients in a client agreement or any other document signed or statement made by the client, are prohibited. The ‘no derogation’ clause must be

30 *DBS Bank (Hong Kong Limited) v. San-Hot HK Industrial Company Limited and Hao Ting* (see footnote 19, above).

31 *Li Kwok Heem John v. Standard Chartered International (USA) Ltd* (see footnote 24, above).

32 *Chang Pui Yin v. Bank of Singapore Ltd* HCCL 12/2013 [2016] (see footnote 23, above).

included in all client agreements unless no client agreement is required because the client qualifies as an institutional professional investor or a qualified corporate professional investor. Hence, the clause is always required when dealing with individuals, or when dealing with corporate professional investors who do not meet the investor knowledge and experience assessment requirements under the Code of Conduct. Thus, suitability requirements have become non-derogable contractual terms in agreements with investor clients.

X LOOKING AHEAD

At some point, the SFC's 'no derogation' clause will be tested in future mis-selling litigation by private and retail bank customers. While there remains an absence of class actions and group litigation orders, and risk is booked to their London or New York affiliates by Hong Kong banks, it is likely to remain the case that there is less institutional litigation involving banks. What the future of class actions and group litigation orders in Hong Kong and the growth of Chinese banks in Hong Kong will mean remains to be seen.

INDIA

*Sonali Mahapatra and Raghuv eer Parthasarathy*¹

I INTRODUCTION

The banking sector in India continues to focus on addressing the sizeable volume of non-performing assets (NPAs) and stressed assets prevalent in the system. The NPAs and the stressed assets in the banking sector have been under scrutiny since 2015 when the Reserve Bank of India (RBI) (the banking sector regulator) initiated an asset quality review (AQR) with a view to ascertain their actual quantum in the banks' books. The AQR exercise revealed that many banks were not appropriately classifying loans as NPAs and were under reporting stressed assets. Following the AQR, RBI fortified the regulatory framework, and put in place measures to enable banks to deal with NPAs and stressed assets. Some of the measures were prudential in nature wherein RBI directed the banks to classify the loans appropriately and provide better provisioning for suspected stressed assets. Separately, the recently enacted Insolvency and Bankruptcy Code 2016 (IBC) has emerged as a viable option for the banks to pursue resolution of NPAs and stressed assets, as it offers a time-bound resolution framework. Subsequent to the enactment of the IBC, the Indian government empowered RBI to direct banks to refer cases under the IBC. Pursuant to such empowerment, RBI began directing the banks to refer a number of large corporate borrowers for corporate insolvency resolution process (CIRP) under the IBC.²

As a result of RBI's initiatives, there has been an increased uptake in banks utilising the IBC with a view to clean up their balance sheets and to realise the best value for their assets. Given the high volume of NPAs in the Indian economy, we expect to see numerous cases go for resolution under the IBC.

i Legislative and regulatory changes

Stressed assets

RBI had traditionally offered banks certain provisioning benefits on restructured assets if certain thresholds were met. Banks and financial institutions often utilised these measures to avoid provisioning for stressed assets and kept these assets marked as standard in their books. RBI has since issued a general circular³ to banks providing that as soon as there is a default

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2 www.livemint.com/Industry/WYSqqL6dHMhxFkjuMFUjSL/Banks-set-to-crack-down-on-defaulters-in-RBIs-second-list.html; most of these companies have now been referred for CIRP under the IBC.

3 RBI Circular No. DBR.No.BPBC.101/21.04.048/2017-18 dated 12 February 2018 on 'Resolution of Stressed Assets-Revised Framework'.

on any account, the lenders must initiate steps to cure the default in the form of a resolution plan. For large accounts,⁴ RBI has specified that the resolution plan must be implemented by the later of six months from the date of default and 30 September 2018, failing which the lenders must refer the borrower for CIRP under the IBC within 15 days from the expiry of the timeline mentioned above. For smaller accounts, RBI proposes to announce the time frame for implementation of resolution plans or a reference under the IBC within the next two years.

ii The IBC

In 2016, the Indian government completely overhauled the existing insolvency regime by enacting the IBC. Since coming into effect, the IBC has been amended twice – once through the Insolvency and Bankruptcy Code (Amendment) Act 2017 (the IBC Amendment Act) and subsequently through the Insolvency and Bankruptcy Code (Amendment) Ordinance 2018 (the IBC 2018 Ordinance) – in each case, to address specific interpretational issues that have arisen in the course of its existence. The IBC 2018 Ordinance (the most recent amendment to the IBC) was introduced to balance the interests of various stakeholders – specifically to safeguard homebuyers and micro, small and medium-sized enterprises, and to promote resolution of assets over liquidation by reducing thresholds for voting by the committee of creditors. The key features of the IBC Amendment Act and the IBC 2018 Ordinance are:

- a eligibility criteria for resolution applicant: initially, the IBC did not bar promoters and other shareholders of a corporate debtor from participating in the resolution process and permitted such promoters and shareholders to bid for and re-acquire the corporate debtor (typically at a discount). This was widely perceived as being unfair as it was felt that errant promoters should be held responsible for the state of their companies. The IBC Amendment Act now renders certain persons ineligible to submit resolution plans if such persons are not compliant with the conditions stipulated in Section 29A of the IBC, which include resolution applicants being, or having connected persons that are, *inter alia*, undischarged solvents, wilful defaulters, in management of or in control of any corporate debtor whose debt has been a non-performing asset for a year or more and persons who have issued guarantees that remain unpaid after invocation;
- b the IBC, pursuant to the IBC 2018 Ordinance, provides that any amount raised from an allottee under a real estate project registered under the Real Estate (Regulation and Development) Act 2016 will be considered as financial debt. Prior to this amendment, the Supreme Court of India had previously taken cognisance of the requirement to protect interests of homebuyers in *Chitra Sharma v. Union of India*⁵ and directed that the interim resolution plan should make all necessary provisions to protect the interests of the homebuyers. The Supreme Court also directed a counsel to be appointed to participate in the meetings of the committee of creditors under Section 21 of the IBC to espouse the cause of the homebuyers and protect their interests;
- c a CIRP application can now be withdrawn even after the National Company Law Tribunal (NCLT) has admitted it, provided that such withdrawal is approved by creditors having 90 per cent of the voting rights in the committee of creditors. Previously, parties had to approach the Supreme Court to withdraw CIRP applications;

4 Defined as accounts where the aggregate exposure of the lenders is 20 billion rupees or more.

5 [2018] 147 SCL 75 (SC).

- d* operational creditors were previously required to provide a statement of account from the bank with which they maintained accounts, certifying that the operational debt was unpaid at the time of filing an insolvency application before the NCLT in relation to any corporate debtor. This was becoming difficult to provide, especially for foreign operational creditors who did not have bank accounts in India. The IBC 2018 Ordinance has eased this requirement such that operational creditors can now provide bank statements, records with any information utility or such other evidence as may be available, to prove that the debt is outstanding;
- e* to ease the decision-making process of the committee of creditors, voting thresholds have been brought down. Important decisions such as approving a resolution plan or replacing an insolvency resolution professional now require a vote of 66 per cent of voting shares, as opposed to the previous threshold of 75 per cent. All other decisions can be taken by a vote of 51 per cent of voting shares; and
- f* purely financial entities, such as banks, foreign portfolio investors and alternative investment funds have been allowed certain exemptions from the criteria set out for persons ineligible to be resolution applicants.

II SIGNIFICANT RECENT CASES

Given that the IBC has come into force recently, the jurisprudence under it has just started evolving and each decision explores a new area of interpretation. A few key areas that banks should be aware of, based on decisions seen so far, are:

- a* eligible bidders in the case of a sale pursuant to an insolvency resolution plan;
- b* time periods to be excluded from the total period of resolution process; and
- c* the ability of creditors to initiate insolvency proceedings against guarantors.

i Eligibility of bidders

At the time of the last edition of this review, the IBC had been recently notified and companies had just begun to have insolvency proceedings admitted against them. Since then, numerous companies admitted for insolvency have had resolution plans implemented. One key obstacle to the finalisation and implementation of resolution plans has been the objections raised by losing bidders in relation to the eligibility of the winning bidders and the manner in which the bid process was conducted by the resolution professional and the committee of creditors. Set out below are some recent examples of this type of litigation.

In *Bank of Baroda v. Binani Cement Limited and ors (Binani)*,⁶ the corporate debtor, Binani, was admitted for CIRP under the IBC on account of its failure to repay a loan availed from Bank of Baroda. Pursuant to commencement of the CIRP, other cement companies in India submitted resolution plans for Binani. In the bidding war that ensued, the consortium led by a cement player, Dalmia Bharat Limited, emerged successful, and the resolution plan submitted by Dalmia (through its subsidiary Rajputana Properties Private Limited) was selected by the committee of creditors of Binani (Binani CoC). UltraTech Cement Limited, another cement player and an unsuccessful resolution applicant, challenged the selection of Dalmia's resolution plan by the Binani CoC. One of the key contentions of UltraTech was that the Binani CoC and the insolvency resolution professional (Binani IRP) appointed

⁶ CA (IB) No. 201/KB/18.

for the CIRP of Binani did not consider UltraTech's revised offer (which was higher than Dalmia's offer) on technical grounds, and that UltraTech's revised bid offered a much better recovery for Binani's lenders. The Binani CoC and the Binani IRP had refused to consider the revised offer, as the submission of such revised offer: (1) was not in accordance with the guidelines stipulated by the Binani IRP; and (2) was submitted after the expiry of timelines prescribed by the Binani IRP. The NCLT ruled that the grounds on which the Binani CoC rejected UltraTech's revised offer were not substantive, and directed Binani CoC to consider UltraTech's revised offer (and provide an opportunity for Dalmia to match UltraTech's revised offer) on the basis that a committee of the creditors under the IBC is required to ensure 'maximisation of value of assets' of a corporate debtor. Dalmia has appealed to the National Company Law Appellate Tribunal (NCLAT) against the NCLT's order, which has directed that the process of selecting a final bidder continues, subject to its decision in this matter. Dalmia has also appealed to the Supreme Court against the NCLAT order. The Supreme Court has directed the resolution process to continue but has refrained the Binani CoC from finalising the bidder until it has issued its decision.

The decision of the Supreme Court on the eligibility of UltraTech's bids is keenly awaited as it is likely to be a bellwether on whether the sanctity of the CIRP process under the IBC will be upheld or pragmatism of dispensing with such process may be preferred, in order to obtain optimal outcomes for the stakeholders.

In *State Bank of India v. Electrosteel Steels Limited*,⁷ Renaissance Steel Private Limited (RSPL) (an unsuccessful resolution applicant) challenged the selection of Vedanta Limited as a successful resolution applicant by the committee of creditors of Electrosteel that was admitted for CIRP under the IBC. The challenge was on the basis that Vedanta was ineligible, under Section 29A(d) of the IBC, to submit a resolution plan. A person is ineligible to submit a resolution plan under Section 29A(d) if such person or a connected party has been convicted of any offence punishable with imprisonment for two years or more.⁸ In this case, a foreign subsidiary of Vedanta's parent had been convicted of violation of environmental laws in Zambia, which was punishable with both imprisonment and a fine. Although the relevant subsidiary was only subject to fines, RSPL contended that this should disqualify Vedanta from bidding for Electrosteel.

The NCLT, citing a precedent from the Supreme Court, held that there is a distinction between an offence that is punishable with an: (1) 'imprisonment or fine'; and (2) 'imprisonment and fine', and stated that the former is a 'less serious offence' than an offence that is solely punishable by imprisonment. On this basis, the NCLT held that the subsidiary's offence would not result in Vedanta being ineligible under Section 29A(d), and approved the implementation of Vedanta's resolution plan. RSPL has appealed to the NCLAT against this order from the NCLT. The NCLAT has ordered the parties to act in terms of the resolution plan (which has been approved by the NCLT), and Vedanta (being the successful resolution applicant) has been permitted to deposit upfront amounts payable to the lenders

7 CA (IB) No. 227/KB/2018.

8 This sub-section was subsequently amended by the IBC 2018 Ordinance under which a resolution applicant will be ineligible to submit a resolution plan under the IBC, if such applicant or a connected person is convicted for any offence punishable with imprisonment for: (1) two years or more under specific Indian legislation (listed in the IBC); or (2) seven years or more under any law for the time being in force. The amended provision also lists other exceptions and carve-outs.

of Electrosteel. The NCLAT has ordered that if the appeal is eventually decided in favour of RSPL and the resolution plan is set aside, then the committee of creditors will have to refund these amounts.⁹

In addition to the above, there are a number of cases where banks have referred large corporate borrowers who have defaulted on loans for resolution under the IBC. For instance, the CIRP was initiated against Essar Steel Limited (one of the largest steel companies in India) in July 2017 and is yet to be completed, primarily because prospective bidders have consistently delayed the process by approaching the NCLT to disqualify other bidders under one or more grounds prescribed under Section 29A.

Most of the cases relating to large corporate borrowers are still being resolved and a common feature across all such cases has been the intense litigation at each level initiated either by unsuccessful bidders or by existing owners (in a bid to buy back the corporate debtor). Consequently, managing the CIRP under the IBC will be a key pressure point for banks. Disgruntled bidders, promoters and other affected parties are likely to try to hamper the running of the process by challenging winning bids – especially if the borrower is a large corporate and this is likely to continue as a major source of litigation going forward.

ii Time periods to be excluded from the total period of resolution process

Under the IBC, once an insolvency petition is admitted against a corporate debt, the resolution plan must be implemented within 180 days, or 270 days (if a one-time extension of 90 days is availed by the committee of creditors) of CIRP being initiated (insolvency resolution period).¹⁰ If a resolution plan is not implemented within this time, then the company is compulsorily liquidated. The importance of completing the resolution process within the insolvency resolution period was emphasised by the Supreme Court in *Innovative Industries Limited v. ICICI Bank & Anr.*¹¹

In view of the strict timelines imposed by the IBC for implementation of a resolution plan, the question of how to treat the time spent by the parties in litigating a matter under the IBC becomes important. No clear principles have emerged yet on this issue, and NCLTs and NCLATs, on an ad-hoc basis, have been providing specific exceptions for excluding certain periods from the calculation of the insolvency resolution period.¹²

In *Quinn Logistics India Pvt Ltd v. Mack Soft Tech Pvt Ltd & Ors*,¹³ the NCLAT, while considering a request for excluding a period of 166 days from the count on account of the CIRP being stayed by an interim order passed by the NCLT, has set out a list of illustrative situations in which the time period intervening the insolvency resolution period can be excused from the count.

9 *Renaissance Steel India Private Limited v. Electrosteel Steel Limited*, Company Appeal (AT) (Insolvency) No. 175 of 2018.

10 Section 12 IBC.

11 AIR 2017 SC 4084.

12 For instance, see *Quantum Limited (Corporate Debtor) v. Indus Finance Corporation Limited*, Company Appeal (AT) (Insolvency) No. 35 of 2018; *Amar Remedies Ltd (Through the Resolution Professional) v. IDBI Bank Ltd & Ors*, Company Appeal (AT) (Insolvency) No. 59 of 2018; *M/s Shilpi Cable Technologies v. Macquarie Bank Ltd*, IA No. 30 of 2018 in Company Appeal (AT) (Insolvency) No. 101 of 2017.

13 Company Appeal (AT) (Insolvency) No. 185 of 2018.

These are as follows:

- a the CIRP being stayed by a court of law or relevant adjudicating authority under the IBC;
- b the resolution professional not functioning for any reason during the CIRP;
- c the period between the date of order of admission or moratorium and the date on which a resolution professional assumes charge of the CIRP;
- d the period for which an order is reserved by the relevant adjudicating authority under the IBC and is subsisting until an order is passed enabling the resolution professional to complete the CIRP;
- e the period for which the CIRP is set aside by the relevant adjudicating authority under the IBC and until such order is reversed by an appellate authority; and
- f any other circumstance that justifies exclusion of a certain period.

iii Ability of creditors to initiate insolvency proceedings against guarantors and security providers

Under Section 14 of the IBC, once an insolvency petition is admitted against a corporate debtor, a moratorium comes into effect during which no actions to foreclose, recover or enforce any security interest created by the corporate debtor can be undertaken.¹⁴ One of the most vexing issues that has emerged in the past year from the interpretation of the IBC is in relation to the treatment of guarantees and third-party security provided to lenders, when the principal debtor is undergoing CIRP under the IBC.

The wording of Section 14 is fairly clear in that it applies to security interests over the assets of the corporate debtor. However, there have been differing judgments from the NCLT, NCLAT and High Courts on the ability of the creditors to initiate enforcement proceedings against guarantors or third-party security providers while the principal debtor is undergoing CIRP. In several instances, the NCLT, NCLAT and High Courts have not permitted separate enforcement proceedings to be initiated against the guarantors when the principal debtor was undergoing CIRP.¹⁵ On the other hand, the NCLT and NCLAT have also clarified that moratorium under Section 14 does not extend to the properties of a guarantor, which have been mortgaged (and sought to be enforced by the lender) since the IBC refers to 'its' assets, being the corporate debtor's assets.¹⁶

Additionally, doubt was also cast on the status of bank guarantees and the ability to enforce them during the moratorium period. Outside of the IBC, courts have consistently held that bank guarantees are independent obligations undertaken by banks and can be enforced without reference to the underlying obligations, subject to absence of fraud in obtaining the guarantee or where invoking the guarantee leads to irreparable harm. In *Nitin Hasmukhlal Parikh v. MG VCL*,¹⁷ the NCLT held that bank guarantees provided towards

¹⁴ Section 14 IBC.

¹⁵ For instance, see *State Bank of India v. Sanjeev Shriya* [2017] 144 SCL 545 (All); *State Bank of India v. M/s Vecons Energy Systems Private Limited & Ors*, Company Appeal (AT) (Insolvency) No. 213 of 2017. Also see *IDBI Bank Limited v. BCC Estate Private Limited*, where the NCLT held that CIRPs that have commenced against a principal debtor will not restrict insolvency resolution proceedings being initiated against the corporate guarantor for the default of the guarantee debt, given that the guarantor is an independent entity.

¹⁶ For instance, see *Alpha & Omega Diagnostics (India) Limited v. Asset Reconstruction Company of India Limited*, Company Appeal (AT) (Insol) No. 116 of 2017; and *Schweitzer Systemtek India Pvt Ltd And Ors*, Company Appeal (AT) (Insol) No. 129 of 2017.

¹⁷ [2018] 146 SCL 412.

a security deposit to be provided by the corporate debtor to MGVCL (a customer of the corporate debtor) cannot be encashed by the customer, while performance bank guarantees provided by banks on behalf of the corporate debtor can be encashed. The rationale adopted by the NCLT is that 'performance guarantees' have been specifically carved out of the definition of 'security interest' in the IBC, but other bank guarantees have not.

Section 14 has now been amended by the IBC 2018 Ordinance expressly clarifying that moratorium imposed under Section 14(1) will not be applicable to a surety in a contract of guarantee to a corporate debtor, which ought to remove the lack of clarity on enforcement of guarantees. The amendment should also cover bank guarantees; however, because of the interpretation of the NCLT that bank guarantees (other than performance guarantees) constitute a security interest, it remains to be seen how cases decided after the IBC 2018 Ordinance coming into force will treat bank guarantee. The IBC 2018 Ordinance does not clarify the applicability of moratorium to enforcement proceedings initiated against third-party security providers.

The other difficulty in relation to guarantees has arisen in scenarios where a CIRP has been initiated in respect of the guarantor. The definition of 'financial debt' in the IBC clearly includes guarantees of financial debt. No distinction has been made between financial creditors claiming under an ordinary debt and those claiming under a guarantee debt.¹⁸ However, in *Axis Bank Limited and Ors v. Edu Smart Services Private Limited*,¹⁹ the NCLT interpreted the definition of the term 'claim' under the IBC to exclude any claims under a guarantee by a beneficiary unless the guarantee has been 'invoked' and a demand has been made on the guarantor. Consequently, if a CIRP is initiated against the guarantor, then the beneficiary must necessarily invoke the guarantee before the petition is admitted and the moratorium comes into effect. The NCLT has also held that invocation of a guarantee provided by a company is restricted once a CIRP is admitted against that company. These decisions have been appealed to the NCLAT.

III CHANGES TO COURT PROCEDURE

Commercial courts

In 2015, the government passed the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Act 2015 (the Commercial Courts Act). The Commercial Courts Act provides for setting up commercial courts at a district level and setting up commercial divisions and commercial appellate divisions in Indian High Courts. These courts will deal with commercial disputes, which will include 'disputes arising out of ordinary transactions of merchants, bankers, financiers and traders such as those relating to mercantile documents, including enforcement and interpretation of such documents'. The idea behind the Commercial Courts Act is to speed up resolution of commercial disputes in India and, to that effect, the Commercial Courts Act has various provisions (on process and

¹⁸ Where an amount claimed by a creditor is not precise, owing to any contingency or other reason, the regulations governing CIRP issued under the IBC (CIRP Regulations) requires the resolution professional to make the best estimate of the claim. Given the above, as per the CIRP Regulations, all that the beneficiary of a guarantee to register a claim in the insolvency resolution process of a guarantor should have to do is to: (1) provide copies of the guarantee and the facility documents; and (2) financial statements showing that the debt has not been repaid either by the principal debtor or the guarantor.

¹⁹ [2017] 205 CompCas 403.

timelines) that, if enforced, would have the effect of streamlining processes and reducing timelines for resolution of disputes. However, given that banks already have recourse to debt recovery tribunals and to NCLTs (under the IBC) to address their disputes, the impact of the Commercial Courts Act on banks may be limited.

The Indian government recently introduced the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts (Amendment) Ordinance 2018 (the Ordinance) to amend the Commercial Courts Act. These amendments have reduced the minimum value of disputes (to determine pecuniary jurisdiction) to 300,000 rupees, thereby bringing more matters into the purview of the commercial courts. The Ordinance also introduced a mandatory pre-institution mediation for suits not requiring urgent interim relief.

IV SOURCES OF LITIGATION

In terms of litigation against banks, common causes have included: (1) failure or delay in repaying deposits; (2) wrongful dishonour of cheques; (3) refusal to grant loans; (4) failure or delay in paying bank guarantees; (5) charging interest at rates higher than those stipulated in the loan agreement; and (6) deficiency in service on various other matters.

In addition to the above, for the next couple of years, banking litigation in India is likely to, in large part, revolve around IBC proceedings and matters ancillary thereto (such as resolution of assets, creditor rights *inter se*, etc.). We have already seen jurisprudence around the IBC evolve substantially since it was enacted and as banks and other creditors continue to make the IBC their first port of call to resolve NPAs and stressed assets, we expect to see the jurisprudence around the IBC evolve even more.

V LAWYER–CLIENT PRIVILEGE

The Indian Evidence Act 1872 (the Evidence Act) attaches privilege to communication made during the course of professional employment to legal practitioners, against disclosure of any advice given to the client or against disclosure of communication made during the course of his or her employment. The privilege continues even after the employment has ceased. The protection is given to what might constitute legal advice and not to any other communications from the adviser. In addition, such protection is not granted to the disclosure of any communication made in furtherance of any illegal purpose or the disclosure of any fact observed by the legal practitioners in the course of employment, in case a crime or fraud has been committed since the commencement of his or her employment (as opposed to before the employment commenced).

The law further provides that a person cannot be compelled to disclose to a court any confidential communication that has passed between that person and his or her legal professional adviser. However, where such person voluntarily offers himself or herself as a witness, he or she may be compelled to disclose such communications to the court that appear necessary in order to explain any evidence that he or she has given.

The privilege under the Evidence Act also extends to the contents or condition of documents with which the legal adviser becomes acquainted in the course and for the purpose of his or her professional employment. Communications containing facts of a matter for the benefit of the legal adviser that are shared for the purpose of seeking legal advice may enjoy privilege.

The principle of litigation privilege – that privilege is attached to any document prepared for the purposes of, or in anticipation of, litigation – recognised under English law, is not reflected in the Evidence Act. This common law principle has, however, been recognised by the Bombay High Court.²⁰ In that case, the management of the company had directed for studies to be conducted by its advertising and public relations departments. It was held that the company was entitled to claim legal privilege on the internal communications with the legal and other departments because the documents were brought into existence with the sole purpose of obtaining legal advice. This decision seems to suggest that if any work has been commissioned for the purpose of seeking legal advice, such work product in the form of a document will enjoy privilege.

VI JURISDICTION AND CONFLICT OF LAW

In contracts where one of the parties is foreign, Indian law generally allows the parties to decide the forum²¹ and the governing law of the contract.²² Parties have the option of submitting to the exclusive jurisdiction or non-exclusive jurisdiction of courts within whose jurisdiction they reside or a neutral forum (i.e., a forum not having a nexus with either of the parties to the contract). The only exception to the rule is if the forum chosen violates domestic law or is against public policy.

Other than judgments of superior courts in reciprocating territories,²³ foreign judgments cannot be automatically executed in India. To enforce foreign judgments from non-reciprocating territories, the judgment creditor will have to file a fresh suit in a domestic Indian court of competent jurisdiction, on that foreign decree or on the original, underlying cause of action, or both.²⁴ However, foreign judgments are considered conclusive as to the matters adjudicated upon as part of the judgment.

Both the execution of judgments from superior courts in reciprocating territories and the conclusiveness of judgments from non-reciprocating territories can be challenged on certain grounds, including: (1) the judgment not being given by a competent court; (2) the judgment not being on the merits of the case; (3) the judgment being founded on an incorrect view of international law or refusal to recognise Indian law, in cases where such laws are applicable; (4) when the proceedings in which the judgment was obtained are opposed to natural justice; (5) the judgment being obtained by fraud; and (6) where the judgment sustains a claim founded on a breach of any law in force in India.

20 *Larsen and Turbo v. Prime Displays Ltd and others*, 2002 (5) Bom CR 158.

21 *Modi Entertainment Network and Anr v. WSG Cricket Pte Limited*, AIR 2003 SC 1177; *Piramal Healthcare Limited v. DiaSorin SpA* 172 (2010) DLT 131; *M/s Gupta Coal India Private Limited v. M/s Swiss Marine Services SA* 2014(4)ABR353; *Sunrise Industries India Limited v. PT OKI Pulp and Paper Mills and Ors* 2017 GLH (2) (226).

22 *National Thermal Power Corporation v. Singer Company*, AIR 1993 SC 998, the only limitation to this rule is that the intention of the parties must be expressed *bona fide* and should not be opposed to public policy.

23 Some of the reciprocating territories are: Bangladesh, Hong Kong, Papua New Guinea, Singapore, Trinidad and Tobago and the United Kingdom.

24 *Marine Geotechnics LLC v. Coastal Marine Construction & Engineering Ltd* 2014 (2) Bom CR 769.

VII LOOKING AHEAD

The Indian government has recently introduced amendments to the Specific Relief Act 1963, which are yet to come into effect. The key takeaway from the amendment bill is that it makes specific performance of contracts the rule rather than the exception. Under the new amendments, the promisee (the aggrieved party), has a right to have the (breached) contract performed through a third party or by his or her own agency. The promisee can then recover the expenses and other costs incurred for such 'substituted performance' from the promisor (the defaulter). Although the amendment specifically clarifies that exercising such substituted performance does not limit other rights of the aggrieved party, such as claiming compensation, it conveys a clear message that specific performance should be adhered to as a rule.

Separately, the amendment bill proposes to include a new provision in the Specific Relief Act under which the courts are not permitted to grant injunctions in a dispute involving contracts relating to infrastructure projects (separately defined in the amendment bill) if granting of such injunctions would impede or delay the progress or completion of such projects. Additionally, the amendment bill proposes to designate certain civil courts as special courts to try suits under the Specific Relief Act in respect of contracts relating to infrastructure projects.

ITALY

*Alessandro Villani and Francesco Amatori*¹

I SOURCES OF LITIGATION AND SIGNIFICANT RECENT CASES

Litigation against banking institutions continues to experience a constant growth in Italy. The most common legal issues, analysed in last year's edition of this review, that constitute the subject matter of proceedings against banks are:

- a* contractual usury;
- b* supervening usury;
- c* indexation to a foreign currency in loan agreements; and
- d* correct indication in a loan agreement of the relevant annual percentage rate of charge (APR).

In addition, another hot topic in banking litigation relates to the interpretation of 'written form' for the purposes of Article 23 of the Italian Financial Act (TUF), recently clarified by the United Chambers of the Supreme Court (the United Chambers) in a landmark ruling.

i Contractual usury

Under Law No. 108/1996 of 7 March 1996, a financing agreement shall be considered usurious (and the relevant clause or clauses null and void) when interest and other lending-related costs, collectively considered, exceed a maximum threshold. Such threshold (different for each credit product category) is quarterly determined on the basis of the average global interest rates applied by lending banks and intermediaries who shall periodically communicate the global rates applicable to the Ministry of Economy and Finance in accordance with the instructions issued by the Bank of Italy. As analysed in last year's edition of this review, one of the main issues Italian courts have to deal with in applying this regime is the exact identification of the items (i.e., interest and other lending-related costs) that have to be collectively measured against the quarterly maximum threshold for the purposes of the usury test.

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One of the items the inclusion of which was (and still is) frequently discussed in court is the contractually provided nominal default interest rate, deemed by almost all Italian lower courts² not to be added to the relevant financing lending-related costs, mainly because:

- a default interest represents an *ex ante* and presumptive determination of damages potentially caused by late repayment of a monetary obligation, the actual accrual and amount of which is subject to the obligor's delay (if any) in paying the amount due, while interest and other costs and expenses to be paid by a borrower as consideration for the amount made available to the same by a lender – and not as a result of any borrower's potential conduct during the course of the contractual relationship – are considered to be the actual lending-related costs to be cumulated and collectively measured against the relevant usury threshold; and
- b default interest is an item not included in the average global interest rates, to be communicated to the Bank of Italy by banks and intermediaries pursuant to the same banking authority's instructions for the purposes of determining the quarterly usury threshold. Therefore, based on the 'symmetry principle' (analysed in detail in last year's edition of this review and recently supported by Supreme Court decision No. 12965/2016), default interest shall not be included in the items to be cumulated and collectively measured against the relevant usury threshold.³

In addition, a material number of case law precedents have held that default interest, given its 'interest' nature, shall in any case be individually and separately measured against the above-mentioned maximum threshold for the purposes of a usury test parallel to the one relating to lending-related costs.⁴

However, some doubt has recently been cast on the just described (and almost unanimously applied) principles (1) after the Supreme Court issued decisions Nos. 5598/2017 and 23192/2017, stating (with quite enigmatic words) that the usury threshold 'relates to both interest provided for as consideration and default interest' and, therefore, the argument according to which it is not allowed to cumulate these two interest rates is not enough to exclude usury; and (2) upon recognition of a case law contrast on the existence in the Italian legal system of the above-mentioned 'symmetry principle' applicable to the usury test, by Order No. 15188/2017 requested to its United Chambers confirmation on this specific issue.⁵

That said, a careful reading of the decisions under item (1), above, reveals that the doubts cast in relation to the regime applicable to default interest, for the purposes of the usury test, were – as unfortunately happened in the past in relation to Supreme Court

2 See, *ex multis*, Court of Milan decision No. 302 of 8 March 2016; Court of Rome decision No. 16860 of 16 September 2014; Court of Padua of 10 March 2015; Court of Bologna of 17 February 2015; Court of Turin decision No. 5984 of 17 September 2014; and Court of Naples decision No. 5949 of 15 April 2014.

3 It is worth reminding that, pursuant to the symmetry principle, consistency between the items to be taken into account for the calculation of, on the one hand, the global lending cost rate relating to a single contract, and, on the other hand, the relevant threshold value to be complied with, is necessary to avoid the risk of comparing two non-homogeneous figures.

4 See, *ex multis*, Court of Milan of 12 February 2015, Court of Padua of 10 March 2015 and Court of Mantua decision No. 1026 of 13 September 2016.

5 Even though the case to be adjudicated by the Supreme Court relates – as per the previously mentioned decision No. 12965/2016 – to the inclusion of a specific banking overdraft fee (called CMS) in the usury test relevant items.

decision No. 350/2013 – originated by a mere misinterpretation of the same. In fact, as also pointed out by case law subsequent to the 2017 decisions at hand,⁶ in such cases the Supreme Court set aside the then challenged lower courts' judgments on the basis of the fact that the latter never actually measured the contractually provided default interest rates against the usury threshold applicable at the time of the entry into the relevant agreements, but rather they excluded such threshold to have been exceeded on the basis of the mere theoretical impossibility to cumulate actual lending-related costs and default interest for the usury test purposes.

Therefore, subject to the United Chambers' expected ruling on application of the 'symmetry principle' to the contested banking overdraft fee inclusion issue (which, in any case, does not directly involve the default interest inclusion issue, above), no change in usury case law has been brought by the above-mentioned 2017 Supreme Court decisions.

ii Supervening usury

One of the most relevant rulings issued by Italian courts in the past year is decision No. 24675/17 dated 19 October 2017 issued by the United Chambers, which (hopefully) definitively solved the Italian legal issue commonly termed 'supervening usury'.

As analysed in more depth in last year's edition of this review, this expression has been commonly used to describe cases where interest (plus other lending-related costs) provided for in a financial contract, or paid pursuant thereto, exceeds one of the quarterly usury thresholds of Law No. 108/1996, applicable during the relevant contractual period, even though, at the date of the relevant financial contract: (1) Law No. 108/1996 was not yet in force; or (2) the then applicable usury threshold was complied with by interest (plus other lending-related costs) applicable at such date.

Under such circumstances, a few case law precedents had held that interest paid in excess of the applicable usury thresholds had to be *ex officio* reduced by judges to the level of such thresholds on the basis of a (partial) ineffectiveness of the relevant contracts for alleged post-signing violation of Law No. 108/1996.

However, such a violation has now been denied by the United Chambers, who, based on (1) the fact that the usury test shall be performed only with respect to interest (and other lending-related costs) applicable at the date of the agreement; and (2) the non-retroactive effect of Law No. 108/1996, held that the 'supervening usury' does not exist in the Italian legal system. Such landmark decision has been subsequently confirmed by other Supreme Court and lower court rulings,⁷ the latter leaving no further doubts on this utterly delicate matter for all banking businesses in Italy.

iii Foreign currency indexation clauses

With regard to the relatively common issue in Europe relating to the alleged invalidity of foreign currency (mainly Swiss franc) indexation clauses included in residential mortgage loans, Italian courts are gradually aligning with the view expressed by the Court of Milan in decision No. 6520/2017 of 9 June 2017 (analysed in last year's edition of this review).

⁶ See Court of Brescia No. 1191 of 19 April 2018.

⁷ See Supreme Court decisions Nos. 9762/2018 and 2311/2018, as well as Court of Appeal of Milan decision No. 4862 of 21 December 2017 and Court of Avellino decision No. 1028 of 29 May 2018.

In fact, claims pursuant to which such foreign currency indexation clauses are to be considered: (1) a separate and autonomous derivative contract embedded in the mortgage loan; and thus (2) null and void for violation of the bank's obligations relating to investment services and activities to retail clients, have been rejected by an increasing number of recent rulings.⁸

In accordance with the path already outlined by decision No. 6520/2017, above, the core reason behind such subsequent rulings is the clear difference between the socio-economic function⁹ and structure of a derivative contract, and the function and structure of a foreign exchange indexation clause included in a loan agreement. The function of the latter is not – as for derivative contracts – focused on the exchange of a differential in order either to provide hedging of a specific (currency) risk or to speculate on such a risk: the specific function of this clause is to serve the sole purpose of the loan, adjusting repayment flows to the relevant currency exchange rate evolution rather than creating new flows on the basis of such an evolution.

iv Incorrect indication of the APR

The issue relating to the consequences arising from the wrongful indication of the APR – introduced by Council Directive 90/88/EEC of 22 February 1990 – in the context of a loan remains one of the most frequent causes of action in the Italian banking litigation context.

In such respect, the borrowers, upon the wrongful indication or calculation of the APR in their loan agreement, usually claim the relevant interest clause to be null and void for alleged violation of Article 117 of the Italian Banking Act (TUB), which sanctions with invalidity any clause providing for rates and prices less favourable to the client than those communicated by the bank in the pre-contractual phase.

However, on this specific issue, Italian courts have started to follow what has now become the mainstream opinion according to which, in case of incorrect indication of the APR, the relevant interest clauses remain valid. In fact, Article 117 of the TUB is considered not to be applicable to the APR because the latter is a rate used for client information purposes only, and not a specific condition of the loan directly applicable to borrowers.¹⁰

v Written form under Article 23 of the TUF

The last significant case, recently addressed by the United Chambers with decision No. 898/2018 of 16 January 2018, derives from the interpretation of Article 23 of the TUF. This provision imposes an obligation on banks and firms to enter into a written master

8 See Court of Milan decisions Nos. 12332 of 6 December 2017 and 6080 of 30 May 2018; Court of Rome decision No. 20311 of 27 October 2017; Court of Monza of 12 January 2018 (RG No. 83/2015); and, with respect to financial lease agreements, Court of Udine decision No. 296 of 7 March 2018.

9 It is worth reminding that such contractual element represents the grounding of an agreement under Italian law.

10 See, *ex multis*, Court of Milan decision No. 8427 of 28 July 2017; Court of Rome of 23 February 2018 and 19 April 2017; Court of Naples decision No. 183 of 9 January 2018; Court of Mantua of 2 May 2017 and 20 December 2017; Court of Bergamo decisions Nos. 3004 of 5 December 2017 and 2302 of 8 September 2017; Court of Monza decisions Nos. 550 of 13 February 2018 and 2403 of 17 August 2017; Court of Salerno of 31 January 2017; and Court of Busto Arsizio decision No. 1150 of 20 July 2017.

contract with retail clients in the case of provision to the latter of investment (and ancillary) services,¹¹ it being understood that the relevant service agreement not complying with such written form obligation shall be considered as null and void.

That said, in last year's edition of this review, it was noted that, in the Italian market practice, the kind of master agreement above is commonly executed through the exchange between the bank or firm and the relevant client of two copies of the relevant contract, each one signed only by the delivering party.¹² This allowed a number of clients (usually not satisfied by the performance of financial assets suggested by banks) to attempt to challenge the validity of their respective framework agreements for violation of the above-mentioned written form, by avoiding to file their respective copy of the contract (signed by the bank) in the context of the relevant judicial proceedings. The copy of the contract only signed by the client (filed by the bank or firm) is then alleged to amount at best to a written contractual proposal, but certainly not to a fully effective and enforceable written contract between the parties.

These claims, together with few isolated court precedents, created uncertainty in the interpretation and application of the written form requirement under Article 23 of the TUF, until the United Chambers, by the above-mentioned decision No. 898/2018, clarified that the sole copy of the agreement signed by the client, and not by the bank, is sufficient to prove that a valid and binding (written) investment services agreement has been entered into by the parties. The rationale behind such ruling is that the nullity sanction imposed by Article 23 of the TUF is only for retail clients' (and not for public interest) protection purposes and, therefore, no such sanction can be imposed if it is proven that the client signed (and was provided with a copy of) the agreement, the written form of which has the only function of making the client fully understand the content of his or her rights and obligations under the same.

II RECENT LEGISLATIVE DEVELOPMENTS

A brief analysis of recent Italian legislation affecting banks cannot ignore the EU Directive 2014/65/EU on markets in financial instruments (MiFID II) package,¹³ which entered into force on 3 January 2018. Envisaged as a further step to create a sole European financial services market, changes in the banking and financial law introduced by this measure relate, *inter alia*, to:

- a* the need to ensure that financial products are negotiated in duly regulated trading venues;¹⁴
- b* strengthened pre- and post-trade transparency requirements;
- c* the need to limit speculation on commodities markets;
- d* regulation of high-frequency algorithmic trading; and
- e* the need to provide a more effective protection for investors.¹⁵

11 A copy of such written contract having then to be delivered to the relevant retail client.

12 In other words, upon conclusion of the contract, the bank would be in possession of a copy of the investment services agreement signed solely by the client, and the client would be in possession of an identical copy of the agreement with the sole signature of the bank's representative thereon.

13 Composed of Regulation (EU) No. 600/2014 and MiFID II, the latter implemented in Italy through Legislative Decree No. 129/2017.

14 E.g., the new organised trading facility for non-equity instruments has been introduced.

15 Through, among others, product governance, stronger suitability assessments and competent authorities' product intervention.

As a consequence of enactment of such European measures, Italian regulatory authorities have issued updated implementation regulations relating, *inter alia*, to markets¹⁶ and financial intermediaries.¹⁷

That said, it has to be highlighted that Italian MiFID II implementation legislation, together with a number of other 2017 measures,¹⁸ also introduced an evolution of the national regulatory system that governs and incentivises whistleblowing activities. This set of rules, to be complied with by banks and financial institutions, provide a legal framework for, and protect (especially in terms of confidentiality), employees or other individuals collaborating with the involved entity, who report facts potentially amounting to:

- a* one of the crimes listed in Legislative Decree No. 231/2001 as condition for corporate administrative liability (e.g., corruption, bribery, fraud);
- b* a violation of market abuse laws;¹⁹
- c* a breach of national anti-money laundering laws;²⁰
- d* an infringement of rules regulating banking activities;²¹ and
- e* an infringement of rules regulating financial intermediation activities.²²

In order to do so, (1) banks and financial institutions shall adopt specific internal reporting procedures, and (2) *ad hoc* procedures are provided for by the law to allow relevant individuals to directly report to the competent regulatory authorities.

Finally, it is certainly worth mentioning that, since 25 May 2018, the European Union data protection Regulation (EU) 679/2016 (GDPR) has been applicable in Italy. Apart from the major impact the GDPR had (and will have) on the Italian legal system as a whole, it is inevitable that banking activities and litigation will be influenced by a number of the GDPR's provisions on, *inter alia*, data portability, processors' requirements, data privacy impact assessment, data protection officers, etc.

III CHANGES TO COURT PROCEDURE

In the context of banking litigation relating to mortgage loans and other (non-complex) retail business contracts, according to a recent trend, clients are increasingly bringing claims against banks and financial institutions in the form of summary proceedings, pursuant to Article 702-bis of the Code of Civil Procedure.

This special form of proceeding was introduced by Law No. 69/2009 of 18 June 2009 for the purposes of reducing the duration of civil proceedings that only require a summary investigation, through simplification of formalities characterising ordinary proceedings. In order to do so, the 2009 reform envisaged a form of process where, *inter alia*: (1) time limits

16 See the Italian Companies and Exchange Commission (CONSOB) Resolution No. 20249/2017.

17 See CONSOB Resolution No. 20307/2018.

18 Namely, Legislative Decree No. 90/2017 of 25 May 2017 on anti-money laundering and Law No. 179/2017 of 30 November 2017, which join previously enacted Law No. 190/2012 of 9 November 2012 and Legislative Decree No. 75/2015 of 25 May 2015.

19 I.e., Regulation (EU) No. 596/2014 and the relevant Commission Implementing Directive (EU) 2015/2392 of 17 December 2015.

20 I.e., Legislative Decree No. 231/2007 of 21 November 2007, as amended and supplemented by Legislative Decree No. 90/2017.

21 See Article 52-bis and 52-ter TUB.

22 See Article 4-undecies and 4-duodecies TUF.

for procedural activities are halved; (2) all unnecessary formalities in the investigation phase have to be avoided; and (3) the judge has a higher degree of freedom in the admission of evidence, the latter needing, in any case, to always have relevance for the case.

That said, even though the clients' intention to resort to Article 702 *bis* proceedings in order to reduce the time lag between their judicial request and the relevant judgment is understandable, in many cases there is an attempt to use such convenient judicial tool outside its scope of application, as identified by Italian case law.

This is what frequently happens in banking litigation cases needing only a documentary investigation, for such sole reason presumed by clients (plaintiffs) to fall within the scope of Article 702 *bis* of the Code of Civil Procedure. In fact, in order to evaluate whether a case meets the summary proceedings requirements, the judge has to take into account not only the amount of effort required to analyse the evidence the parties intend to rely upon (relatively little in the case of documentary evidence), but also the number and complexity of (1) factual circumstances alleged; (2) legal arguments adduced; and (3) persons, entities or parties involved in the dispute.²³

In light of the above, even though most banking litigation cases only need a documentary investigation, it is self-evident that a relevant majority of the same do not meet the requirements above and, therefore, only in a few cases will the judge decide not to convert²⁴ a case of a banking nature initiated pursuant to Article 702-bis of the Code of Civil Procedure to ordinary proceedings.

IV INTERIM MEASURES

Another interesting trend followed by Italian courts relates to interim injunctions against payment of bank guarantees issued by one or more banks in order to secure correct and timely performance by a party (usually a seller) of its obligations under a contract for the benefit of the other party (usually the buyer).

In accordance with consolidated international market practice, these guarantees provide for payment by the guarantor to the beneficiary:²⁵ (1) upon sole submission of pre-identified documents that must conform to the terms of the guarantee;²⁶ and (2) without such guarantor's obligation being subject to claims or defences by the defaulting party resulting from its contractual relationship with the beneficiary applicant.²⁷ In other terms, the guarantor bank is under no duty to investigate the underlying facts to determine whether

23 See, *ex multis*, Court of Turin of 3 December 2013; Court of Naples of 4 April 2014; Court of Verona of 9 August 2011; and Court of Varese of 18 November 2009.

24 The power of the judge to convert *ex officio* a summary proceeding to an ordinary one is granted directly by the law (see Article 702-ter of the Code of Civil Procedure).

25 Or to the beneficiary's bank who, in case the relevant security package provides for a chain composed of more than one bank or guarantor, applies for reimbursement by the defaulting party's banks after having directly paid the beneficiary.

26 Usually a *pro forma* declaration and a demand for payment to the relevant bank, sometimes accompanied by an expert's report evidencing actual non-performance of the relevant contract.

27 This being an application of the 'independence principle' governing the guarantee, according to which the latter is independent from the underlying contract whose performance is secured through issuance of the same guarantee.

in fact the allegedly defaulting party has breached the contract, the same bank being required only to determine whether the face of the confirming documents comply with the terms of the guarantee.

As in many other jurisdictions, in order to set a limit on the consequences deriving from the overly rigid extension of the above-described independence rule in case an undeserving beneficiary commits any misrepresentation in the documents submitted to the bank, Italian law permits the bank to refuse to honour its payment obligation raising the fraud exception (*exception doli*) where it is *prima facie* evident from the submitted documents (or from any other document in the bank's possession) that payment was fraudulently requested.

That said, in case of request of payment under a bank guarantee of this nature, the allegedly defaulting party can try to oppose payment by way of a pre-proceeding *ex parte* injunctive relief, pursuant to Article 700 of the Code of Civil Procedure. As analysed in last year's edition of this review, the criteria for determining whether to grant such extraordinary remedy are: (1) the *periculum in mora*, in this specific case amounting to a substantial threat that the allegedly defaulting party will suffer imminent and irreparable injury if the injunction is not granted; and (2) the *fumus boni iuris* (i.e., a substantial likelihood that the applicant will prevail on the merits), the latter usually being either that a demand for payment of the bank guarantee confirming the terms of the same has not yet been made, or that a demand, even though in conformity, should not be honoured because of fraud in the underlying transaction.

It is clear that both requirements above are difficult to prove (especially considering the narrow scope of the fraud exception, frequently used as grounds for the interim application), thus implying a potentially very small amount of cases in which the above-mentioned injunctive relief can actually be obtained.

However, in order to avoid the (sometimes very) prejudicial situation in which the guarantor honours its obligation on the basis of *prima facie* valid documents that – upon a subsequent full investigation on the merits at the hearing for confirmation of the *ex parte* injunctive order – are then shown to be the result of fraudulent activities, Italian courts²⁸ started to follow a less strict approach in granting Article 700 *ex parte* (i.e., *inaudita altera parte*) injunctive reliefs. In fact, these interim measures now result in usually being granted even when meeting the two above criteria will probably be denied at the relevant order confirmation hearing, but, at the same time, this solution is favourable to banks that do not have to be concerned about the legal and reputational risks of (1) being considered in breach of the guarantee, and (2) having potentially refused payment on the basis of a believed fraudulent, but subsequently proven legitimate, beneficiary's request.

V JURISDICTION AND CONFLICTS OF LAW

One of the most interesting cases on conflicts of law issues recently addressed by the United Chambers relates to compatibility of punitive damages with the Italian legal system, which may not only affect financial institutions and their litigation, but the system as a whole.

28 E.g., see Court of Milan of 11 December 2013 (RG No. 13056/2013); Court of Milan of 19 November 2013 (RG No. 73674/2013); Court of Milan of 6 July 2017 (RG No. 21635/2017); and Court of Rome decision No. 11955 of 24 November 2017.

The Supreme Court's decision (No. 16601/2017) originates from a request for recognition in Italy of a US court judgment that sentenced an Italian company to pay, among others, damages to a US entity allegedly having a punitive nature.

On this specific issue, it has to be recalled that, in 2007²⁹ and in 2012,³⁰ the same Supreme Court did not grant recognition of judgments similar to the one above on the grounds that punitive damages were contrary to Italian 'public policy' provided for by Article 64 of Law No. 218/1995 of 31 May 1995;³¹ the above on the basis of the argument that the Italian legal system would contemplate damages only as means to restore the *status quo ante*, an actual and proven loss, thus allowing the same to be awarded solely for compensatory and not for punitive purposes.

However, by the 2017 judgment at hand, the United Chambers decided to overrule such opinion on the basis of (1) an evolved understanding of 'public policy' under Article 64, connected with the complex of Italian, European and international common fundamental principles and values; and (2) the polyfunctional nature of damages in modern Italian civil law, which includes the above-mentioned allegedly unlawful punitive function. In light of these arguments, the Court thus stated that a judgment awarding punitive damages can be recognised in Italy if:

- a* such punitive damages can be awarded on the basis of a clear and express provision of law, which allows the (1) *ex ante* identification of the precise conducts punishable with such sanction; and (2) prediction of the potential amount of punitive damages deriving from a certain conduct, setting out quantitative limits to the same; and
- b* there is a proportionality between compensatory and punitive damages, and between the latter and the sanctioned conduct.

VI EXCLUSION OF LIABILITY

In relation to limitation or exclusion of banks' liability, with a view to prevent negligent conducts, it is worth mentioning a recent 2018 Supreme Court's decision³² relating to a case where a bank claimed for payment by its clients of the amount of their old current account balance. The amount of such claim was determined on the basis of the bank's internal documentation evidencing each year's account balance only from 1991 onwards, while all documents referring to previous years were no longer in the bank's possession.

The justification adduced by the bank for such lack of documentation was based on Article 2220 of the Italian Civil Code, which provides for the obligation to keep corporate records for 10 years only.

However, the Court clarified that, in cases like the one at hand, a bank cannot invoke Article 2220 rule in order to be excused from providing evidence of alleged unpaid receivables

29 See Supreme Court decision No. 1183/2007.

30 See Supreme Court decision No. 1781/2012.

31 This being the main requirement to be met under Article 64, which provides that recognition of a foreign judgment is subject to the latter's legal effect not being contrary to Italian public policy. In the past, such extremely broad concept of 'public policy' was identified in the complex of fundamental principles characterising the socio-ethical structure of a national community in a certain point in time, as well as the mandatory principles underlying the most important national legal concepts (see Supreme Court decision No. 1680/1984).

32 No. 4102 of 20 February 2018.

against a client, such failure to keep the relevant documentation amounting to a grossly negligent violation of the sound and prudent management principle applicable to all banks under Article 5 of the TUB.

VII LOOKING AHEAD

While in the last edition of this review, future legislative trends could have been reasonably foreseen, this is certainly not the case at the date hereof. A minor civil procedure reform was enacted through Legislative Decree No. 116/2017 of 13 July 2017 and is expected to enter into force from 2021 onwards, but this – together with other already scheduled legislative measures (mainly coming from the EU)³³ – could only give a flavour of how banking law and litigation is expected to evolve.

On the litigation side, an important part will be played by Italian courts, that are expected to definitively address some of the above-mentioned litigation issues (such as the application of the ‘symmetry principle’ in the usury context), or to confirm current case law trends (e.g., the impossibility to qualify simple foreign currency indexation clauses included in mortgage loans as derivatives).

However, the decisive and most uncertain factor in the equation will obviously be the legislative approach of the new Five Star Movement–Lega government to banking matters. Even though such newly elected executive seems to have the intention of distancing itself from the alleged pro-banks approach adopted by the former Renzi–Gentiloni government, it will, however, be interesting to see if such political statement (together with many others) will withstand the pressure of EU institutions and international markets, also in light of the fact that the Italian economy and employment figures are in need of attracting international investment.

In any case, a huge aid in terms of foreign investment attraction power has been served to Messrs Di Maio and Salvini with Draft Law No. 4453 dated 2 May 2017, which envisages a favourable tax treatment in Italy for sukuk and other shariah-compliant contractual structures that, if enacted, could give birth to a whole new line of business for financial institutions in Italy.

33 E.g., the expected Italian bankruptcy law reform.

JAPAN

*Hironobu Tsukamoto and Hiroyuki Ebisawa*¹

I OVERVIEW

No official statistical data on the number and trend of civil litigation cases involving banks and other financial institutions exists in Japan. It is widely believed, however, that the number of lawsuits between investors and financial institutions, one of the main categories from which banking litigation is generated, has decreased compared to the number of the same immediately following the post-global financial crisis era, after the bankruptcy of Lehman Brothers in 2008. This decrease is largely owing to Japan's recent improved economic situation, which benefits many investors, likely obviating their need to seek judicial redress in many instances. Be that as it may, in recent years, some lawsuits involving the banking sector have been heard, on which Japanese courts have handed down seminal decisions. We introduce those court decisions and recent legislative developments, specifically reforms of Japan's Civil Code, which are likely to substantially affect future commercial litigation, including banking disputes. We also explain the major causes of and procedural issues related to banking litigation in Japan.

II LEGISLATION

i Recent legislative developments

The Amendment to the Civil Code of Japan was enacted by the National Diet in May 2017 and promulgated in June 2017. Most of the amendments will come into effect on 1 April 2020. Since this reform covers a wide variety of civil law issues, it is not feasible to explain it in its entirety in this chapter. Several reforms may substantially affect commercial litigation, including one involving banks. The examples of those reforms are below.

Reform on prescription

Under the current Civil Code, a claim is extinguished if not brought within 10 years of the date on which it became possible to exercise its right, owing to extinctive prescription,² with some exceptions (e.g., where the period of extinctive prescription is shorter than the general rule, such as five years, for a claim arising from a commercial act).³ The amendment, which abolishes the exceptions, introduces a new general rule: a claim will be extinguished the earlier

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2 Article 167, Paragraph 1 Civil Code.

3 Article 522 Commercial Code.

of five years after the claimant becomes aware that the right of the claim can be exercised or 10 years after the right of the claim can be exercised. In addition, the amendment introduces a new suspension on prescription, where the completion of the prescription period for a right and claim is suspended for a certain period, generally one year, if parties agree in writing to negotiate such right and claim.

New restrictions on personal guarantees

The Amendment will impose some restrictions on guarantee agreements entered into by individuals. One of the important restrictions is that a guarantee agreement is not effective if (1) the principal debt of such guarantee agreement is a monetary loan owed by the principal debtor for the debtor's business or (2) such guarantee agreement is a revolving guarantee in which the scope of the principal debts includes the monetary loan owed by the principal debtor for the debtor's business, unless the individual guarantor expresses his or her intent in a notarised document to perform the guarantee obligations within one month preceding the execution date of the guarantee agreement.⁴ Further, if a guarantee agreement falls within the scope of (1) or (2) above, the principal debtor is required to provide certain information, such as the properties and income and expenditures of the principal debtor, to the individual guarantor when the principal debtor asks the individual guarantor to assume the guarantee obligations. A failure to undertake such obligations may cause the guarantee agreement to be subject to cancellation by the guarantor.

Change of statutory interest rates

The current Civil Code and the Commercial Code provide a fixed statutory interest rate of 5 per cent⁵ and 6 per cent per annum,⁶ respectively. The Amendment abolishes those fixed statutory interest rates, and introduces a uniform floating interest rate, which will be 3 per cent when the amendment becomes effective but may be revised every three years in light of the average market interest rate. Most loan agreements involving banks and other financial institutions have a provision under which interest rates are prescribed; therefore, the change of statutory interest rates will generally not affect the practice in banking sector-related litigation as far as such loan agreements are concerned. However, this statutory interest applies to a tort claim, which is one of the main causes for customers to sue their banks and financial institutions, such as a claim of failure to explain, as described in Section VII, below. Therefore, this change may affect litigation involving financial institutions to that extent.

ii Regulatory impact on banking litigation

The regulatory scheme regarding financial institutions, including banks, is generally administered by the Financial Service Agency of Japan (FSA). The Banking Act and the Financial Instruments and Exchange Act (FIEA) are the main regulatory sources of law governing the activity of banks and other financial institutions. Further, the Act on Sales, etc. of Financial Instruments (ASFI) restricts sales activities by financial institutions. In addition

4 This restriction is not applicable if the guarantee agreement is entered into by an individual who is involved in the principal debtor's business (e.g., in the case where the individual is a director of the principal debtor if such debtor is a corporation).

5 Article 404 Civil Code.

6 Article 514 Commercial Code.

to these statutes, various cabinet orders and ministerial orders, as well as the FSA's policy guidelines, are in effect in the financial sector. As these are administrative regulations, their violation does not necessarily impose civil liability on the violating financial institutions. However, Japanese courts frequently refer to such violation in determining civil liability. Furthermore, some provisions directly invoke civil liability on a violation of those regulations, such as liability for damages of financial institutions that fail to explain prescribed information to their customers.⁷

III SIGNIFICANT RECENT COURT CASES

i Inheritance of bank deposit account

Under the Civil Code of Japan, the basic rule of intestate inheritance is that successors are to divide inherited property through deliberation and agreement.⁸ However, the Supreme Court of Japan previously held that monetary rights over a bank deposit account held by a descendant is to be automatically transferred to joint successors to the extent of each successor's statutory share of the inheritance without agreement among the successors when succession occurs.⁹ In its decision dated 19 December 2016,¹⁰ the Supreme Court overruled its precedent, holding that the monetary rights over a bank account jointly succeeded to successors are not automatically divided and are subject to deliberation and agreement by successors. This decision significantly affects banking practice in Japan. Before the decision, one joint successor of a bank account could have demanded the bank to withdraw money from that bank account to the extent of such successor's statutory share of the inheritance. However, this decision requires joint successors to deliberate and agree on how to divide money in a bank account; thus, banks can now await the deliberation and agreement by successors before acceding to successors' demands to withdraw money from the bank account. The Supreme Court affirmed the same rule on time deposits in its decision dated 6 April 2017.¹¹

ii Obligations of banks conducting internet banking business

The Tokyo High Court addressed an issue of obligations of banks that provide internet banking business to their account holders in its decision dated 3 March 2017,¹² where a plaintiff holding a deposit account in a bank sued the bank for damages the plaintiff incurred, asserting that the bank negligently transferred money from the bank account to a third party's account and breached its obligation under the deposit agreement. In this case, the plaintiff argued that someone gained unauthorised access to the plaintiff's online bank account and requested the bank to transfer the money to a third party's account, and that the bank negligently accepted such request and transferred the money, which resulted in the plaintiff's loss. The Tokyo High Court found that the bank took reasonable measures in order to prevent such unauthorised access in advance of such incorrect transfer of the money, referring to the facts that the bank requested its customers to install security software and to change the

7 Article 5 ASFI.

8 Article 907, Paragraph 1 Civil Code.

9 Supreme Court, 20 April 2004, Hei 16 (jyu) No. 670, 214 SAISHŪ MINJI 13.

10 Supreme Court, 19 December 2016, Hei 27 (kyo) No. 11, 70-8 MINSHŪ 2121.

11 Supreme Court, 6 April 2017, Hei 28 (jyu) No. 579, 1673 SAIJI 3.

12 Tokyo High Court, 2 March 2017, Hei 28 (ne) No. 5274, 1525 KINHAN 26.

log-in password for bank accounts, and that implementing general suspension measures of a transfer of money would significantly impair the convenience of bank account holders. The Tokyo High Court rejected the plaintiff's arguments, and concluded that the bank was not responsible for the transfer notwithstanding that the unauthorised access caused certain loss to the plaintiff. This decision gives some insight into the scope of duty for banks conducting internet banking business.

IV PROCEDURAL ISSUES

i General procedure of civil litigation

Japanese civil procedure falls within the category of a civil law system, which is different from court procedures in common law countries such as the United States and the United Kingdom. Further, one feature of Japanese civil procedure, which is relevant to litigation between customers and banks, is that no equivalent to widely available class action lawsuits in the United States and other countries exists in Japan. Having said that, however, the Act on Special Measures concerning Civil Court Proceedings for the Collective Redress for Property Damage Incurred by Consumers (ASMCCP), which came into effect in 2016, changes the class action landscape in Japan: for the first time, in limited circumstances, class action-styled lawsuits may be brought. However, such procedure is to be initiated by a specified consumer organisation qualified by the government, and an individual consumer cannot initiate such procedure.¹³ Further, the application of the ASMCCP is limited to certain claims stipulated thereunder,¹⁴ and certain types of damages, such as loss of profits, are excluded from the scope of recoverable loss.¹⁵ In view of such limited availability, we are currently unaware of any procedures under the ASMCCP, including disputes involving banks and other financial institutions.

In contrast to the class action-style procedure, the alternative dispute resolution (ADR) procedure for disputes regarding financial products has become one of the main avenues for the resolution of financial disputes since its introduction in 2010 under relevant legislation, such as the FIEA and the Banking Act. Customers who have a complaint regarding financial products or financial institutions may bring such complaint either to normal court or to a designated dispute resolution organisation for ADR procedure, which has been established in each category of the financial business sector, such as banking and life insurance, although there are no such designated dispute resolution organisations in some financial business categories. This ADR procedure conducted by a designated dispute resolution organisation has some special features compared to standard ADR. One of the main features of this ADR is that a financial institution cannot refuse this procedure without just cause for doing so, if the customer wishes to seek the resolution through the ADR, rather than through court procedure.¹⁶ Further, in ADR proceedings, a designated dispute resolution organisation may request a financial institution to make a report or to submit books and documents or any other articles, which the financial institution cannot reject without just cause.¹⁷ In

13 Article 3, Paragraph 1 ASMCCP.

14 *Id.*

15 Article 3, Paragraph 2 ASMCCP.

16 For example, Article 156-44, Paragraph 2, Item 2 FIEA.

17 For example, Article 156-44, Paragraph 2, Item 3 FIEA.

addition, unlike normal ADRs where the parties may reject a conciliation proposal by an ADR institution, the financial institution is required to accept such proposal except in certain stipulated situations, such as where it chooses to file a lawsuit on the dispute.¹⁸

ii Interim measures

Under the laws of Japan, three types of interim measures concerning civil procedure exist: provisional seizure of assets, provisional disposition of a disputed subject matter, and provisional disposition that determines a provisional status.¹⁹ Regarding litigation involving banks, provisional seizure of assets is often used, whereby a debtor's or guarantor's assets are temporarily seized to enforce a judgment granting a monetary claim over the assets after the court delivers its formal judgment.

V PRIVILEGE AND DISCLOSURE

i Privilege

While no concept exactly equivalent to attorney–client privilege exists, a similar type of protection over attorney–client communications is available under Japanese civil procedure.

Lawyers bear confidentiality obligations for information obtained from clients under professional ethics, and a breach of such obligations could subject the breaching lawyer to criminal sanctions.²⁰ In connection with such confidentiality obligations, the facts that become known to a lawyer during the course of his or her professional engagement and that should be kept secret, are protected. Specifically, the rights of refusal (1) to give testimony on confidential information of clients²¹ and (2) to produce documents containing confidential information of clients²² are provided under the Code of Civil Procedure. Further, documents prepared exclusively for the internal use of document holders are protected from document production orders issued by courts.²³

ii Disclosure

No 'discovery' or other document or information-exchange process in the course of litigation exist in Japan. Instead, the Code of Civil Procedure provides for courts to make orders regarding document production; however, such orders are only available where a party succeeds in presenting the existence and identity of a document²⁴ and where a necessity to produce the same as evidence exists.²⁵ Further, several statutory exceptions exist under which the other party does not bear the obligation of document production.²⁶ Given the general tendency that courts are prudent in granting orders on motions for document production, no substantial disclosure of documents between parties in civil litigation usually occurs.

18 For example, Article 156-44, Paragraph 6 FIEA.

19 Article 20, Paragraph 1; Article 23, Paragraphs 1 and 2 Civil Provisional Remedies Act.

20 Article 134, Paragraph 1 Criminal Code.

21 Article 197, Paragraph 1, Item 2 Code of Civil Procedure.

22 Article 220, Item 4(c) Code of Civil Procedure.

23 Article 220, Item 4(d) Code of Civil Procedure.

24 Article 221, Paragraph 1 Code of Civil Procedure.

25 Article 181, Paragraph 1 Code of Civil Procedure.

26 Article 220, Item 4 Code of Civil Procedure.

VI JURISDICTIONAL MATTERS

Jurisdiction and conflicts of law issues are not usually disputed in banking litigation in Japanese courts. It should be noted, however, that consumers residing in Japan are generally allowed to file a complaint with Japanese courts against banks and other financial institutions concerning disputes arising from agreements between them, even if such agreements provide for the exclusive jurisdiction of a foreign court.²⁷

VII FREQUENT CAUSES OF ACTION AND LITIGATION SOURCES

There are various types of civil litigation involving banks and other financial institutions. Most such litigation is brought by customers of banks and other financial institutions, such as investors purchasing financial products from banks and the like, and customers who deposit money in their bank accounts. Another major source of banking litigation is for banks and other financial institutions to seek repayment of money against debtors or guarantors under a loan agreement or guarantee agreement, as well as those who seek enforcement of a mortgage right over assets of debtors, etc.

i Lawsuits between investors and financial institutions

One of the major types of litigation between financial institutions, including banks, and customers is those where investors sue the institutions for selling financial products that ultimately result in the investors incurring losses. In those lawsuits, in their complaints, investors seek refunds to the extent of their losses, and their typical arguments include the following:

- a failure to explain the contents and risks of financial products;
- b failure to evaluate the suitability of financial products to investors; and
- c the purchase of financial products by fraudulent means by financial institutions or by mistake by investors.

These arguments often overlap, and are concurrently presented to the court. Each argument's effect differs from the other, as explained below.

Failure to explain the contents and risks of financial products

The ASFI requires financial institutions to explain to its customers certain important information about the financial products stipulated thereunder at or before the time of sale of the financial products to the customer.²⁸ If financial institutions fail to perform such duty of explanation, they will be held liable for the damages suffered by the said customer as a result thereof.²⁹

In addition to the ASFI, the Supreme Court has held that, if a contractual party fails to disclose to the other party information that could affect the decision of whether to enter into the agreement, the other party may claim against that party damages incurred from entering into the agreement as a general tort claim.³⁰ Based on this court precedent, investors often

27 Article 3-4, Paragraph 1; Article 3-7, Paragraph 5 Code of Civil Procedure.

28 Article 3, Paragraph 1 ASFI.

29 Article 5 ASFI.

30 Supreme Court, 22 April 2011, Hei 20 (jyu) No. 1940, 65-3 MINSHŪ 1405.

assert that financial institutions fail to disclose necessary information to them when selling financial products, which constitutes a tortious act and that the financial institutions are responsible for the damages that they incurred.

The fulfilment of this explanation duty is generally considered from two different aspects: the scope of explanation and the manner and extent of explanation. Under the scope of explanation, the court essentially requires the financial institutions to explain the basic structure of the financial products in issue and the risk thereof,³¹ which are essential for investors to make well-informed decisions on the investment of the financial products at their own risk. Concerning the manner and extent of the explanation, the courts consider those factors by referring to, among others, the nature of the financial products and knowledge and experience that the specific investors involved had when the transaction was concluded.³²

Failure to evaluate suitability of financial products to investors

A financial institution is required to evaluate a customer's suitability to a financial product in issue, in light of customer knowledge, customer experience and the state of customer assets or the purpose of the transaction in issue, pursuant to the FIEA.³³ This requirement is called the 'principle of suitability', and the Supreme Court addressed the relationship between this principle of suitability and the liability of the financial institution violating this principle, holding that a material violation of the principle of the suitability, such as where a sales person of a financial institution offered to sell financial products that included excessive risks to such customers, may constitute a tortious act and cause the financial institutions to owe civil liability to the investor.³⁴ This court decision is particularly important in that it affirmed the imposition of civil liability on the financial institutions, even though the principle of suitability is originally considered as a regulatory rule and not a direct cause of civil liability being imputed to financial institutions.

Fraud or mistake by investors

An investor sometimes argues that the contract of purchasing the financial products is void or can be cancelled owing to fraud by a financial institution or an investor's mistake regarding the structure and risks of the financial products. However, courts tend to accept such arguments in only limited circumstances, where, for example, a customer did not understand an essential part of the structure and risk of the financial product in issue owing to failure of the financial institution to perform its duty of explanation.³⁵

ii Lawsuit between non-investor customer and bank

In addition to lawsuits between investors and banks, lawsuits between non-investor customers and banks occasionally arise. In a typical case, customers with bank deposit accounts sue banks for non-performance of their duty under deposit agreements. For example, customers assert that banks reject their requests to withdraw money from their bank accounts without just cause. A typical reason for a bank to do so is that there is a dispute as to who has the legal

31 See, e.g., Supreme Court, 7 March 2013, Hei 23 (jyu) No. 1493, 243 SAISHŪ MINJI 51; Supreme Court, 15 March 2016, Hei 26 (jyu) No. 2454, 1648 SAIJI 1.

32 See, e.g., Tokyo High Court, 19 October 2011, Hei 23 (ne) No. 3584, 1942 KINHŌ 114.

33 Article 40, Item 1 FIEA.

34 Supreme Court, 14 July 2005, Hei 15 (jyu) No. 1284, 59-6 MINSHŪ 1323.

35 Osaka High Court, 12 October 2010, Hei 22 (ne) No. 1476, 1914 KINHŌ 68.

right to withdraw money from the account. Another example of this kind of dispute is where customers allege that banks have negligently allowed a payment of money to be made from their bank account to unauthorised persons, and therefore, the banks remain responsible for paying such money to the customers.

In a recent, interesting court case regarding a dispute between a non-investor customer and a bank, a customer filed a lawsuit against a bank for the transfer of money to an incorrect bank account, asserting that such incorrect transfer of the money caused the customer to incur a loss.³⁶ The Tokyo High Court held that such incorrect transfer constituted a failure of performance under a money transfer agreement between the bank and the customer and that the bank was responsible for the loss incurred by the customer. A unique feature of this court case is that the court determined the amount of damages awarded by referring to Article 248 of the Code of Civil Procedure, which provides that, if damage is found to have occurred, but, owing to the nature of the damage, it is extremely difficult to prove the amount thereof, the court may reach a finding on an amount of damages that is reasonable, based on the entire import of oral arguments and the results of the examination of evidence.

iii Lawsuit between a bank and debtor or guarantor

Another typical litigation source involving financial institutions, especially banks, is litigation related to banks' collection of repayments against a debtor and guarantor under a loan agreement or guarantee agreement. Those lawsuits are usually simple because, in many cases, banks clearly have the right to demand repayment against a debtor and guarantor under the relevant agreement. However, under some circumstances, guarantors assert that they misunderstood or were unaware of material facts related to the debtor and loan agreement in issue and that the guarantee agreement is void owing to such mistake. Under limited circumstances, the courts accept such assertion by the grantor and deny the bank's claim.

Further, this type of lawsuit often concurrently occurs with bankruptcy proceedings concerning the debtor. In those cases, the debtor had typically taken out a mortgage to borrow money from the bank or has a deposit account in the bank with which it has entered into a loan agreement. Therefore, disputes frequently occur as to whether the banks' right on the mortgage and bank account has priority over the bankruptcy proceedings.

VIII LIABILITY

The Consumer Contract Act provides, among others, that clauses are void if they completely exempt a business operator from either liability to compensate a consumer for damages arising from default by the business operator or liability for damages to a consumer that arises from a tort committed during the business operator's performance of a consumer contract.³⁷ Therefore, concerning an agreement between a financial institution and an individual, such clauses are void as long as the individual falls within the scope of a consumer and the agreement constitutes a consumer contract stipulated under the Consumer Contract Act.

Regarding lawsuits between an investor and a bank, if the investor's assertion regarding the damage claimed is established, the investor may seek compensation of damages incurred as long as a proximate causation exists between the bank's conduct and the loss incurred by

36 Tokyo High Court, 14 September 2016, Hei 28 (ne) No. 938, 2323 HANJI 101.

37 Article 8, Paragraph 1, Items 1 and 3 Consumer Contract Act.

the investor. Concerning a bank's failure to sufficiently explain information to the investor, one of the main causes of this kind of lawsuit, courts frequently deduct the damages awarded, factoring in the investor's negligence. In some cases, the courts in fact deducted more than half the amount of the loss from the awarded damages.

IX OUTLOOK AND CONCLUSIONS

As explored in this chapter, the range of civil litigation involving banks and other financial institutions is extensive, and it is a monumental task to thoroughly explain these disputes uniformly. Nevertheless, one highlight of litigation trends involving financial institutions is disputes between customers, including investors, and financial institutions, where customers claim damages for losses incurred owing to certain activity or products provided by the financial institutions. As almost 10 years have elapsed since the global financial crisis in 2008, many court decisions addressing alleged losses claimed by investors have been delivered during that period. As a result, with Japan enjoying economic stability in recent years, at present, the incidence of court cases involving financial institutions has stabilised. However, as economic conditions are rarely static and could rapidly change, careful attention should be given to judicial trends on banking litigation to better prepare for the next new, emerging trend in this field in the coming years.

LIECHTENSTEIN

*Hannes Arnold and Sophie Herdina*¹

I OVERVIEW

Despite being ranked the sixth smallest nation in the world, Liechtenstein's financial centre is of great international importance and has gained a respectable reputation over the recent decades. Because of Liechtenstein's membership in the European Economic Area (EEA) since 1995, and its close economic ties with Switzerland, financial intermediaries located in Liechtenstein benefit from privileged access to both the European Union, by way of freedom to provide services, and to the Swiss economic area, owing to the customs and currency treaty that is in place between the two neighbouring states.

The highly regulated banking sector plays an important role in the Liechtenstein financial centre and adheres to the harmonised *acquis* of financial regulation and consumer protection. Owing to the political continuity and economic stability that Liechtenstein provides as a country of domicile in conjunction with the recent positive market developments, the assets managed by Liechtenstein banks, including their foreign group companies, increased from 234.8 billion Swiss francs by the end of 2016 to 294.3 billion Swiss francs by the end of 2017.²

By virtue of the importance of banks to the financial centre and to the economy of Liechtenstein, and the amount of assets managed by Liechtenstein banks, it does not come as a surprise that disputes that need to be resolved through litigation sometimes arise. In the majority of cases in banking matters, litigation is directed against the banks and not initiated by them.

The majority of legal issues in the field of banking litigation arising in the Liechtenstein courts concern the liability of banks and their bodies for the losses of clients, banking secrecy and issues in connection with asset freezing orders. Moreover, the enforcement of pledges that a bank may hold in assets deposited by clients has led to various disputes.³

II SIGNIFICANT RECENT CASES

Although Liechtenstein is not a common law country and banking law is thus based on statutory law, Supreme Court decisions and relevant rulings of the lower courts do have substantial influence on Liechtenstein law, without creating binding precedence.

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2 FMA Liechtenstein Financial Market Report 2018, 12.
3 OGH 7 May 2010, 03 CG.2009.3, GE 2010, 190.

Further, owing to the fact that the Liechtenstein legal system is partly based on Austrian, as well as Swiss, law, the respective Austrian and Swiss Supreme Court decisions need to be taken into account⁴ when assessing the legal situation in Liechtenstein.

i Risk-bearing in giro transactions

Recently, the Liechtenstein Supreme Court ruled that, in giro transactions, the bank bears the primary risk of executing forged payment orders. Further, it decided that the bank cannot pass its losses incurred by such execution of forged payment orders to its clients by way of the strict risk liability provided for in Section 1014 of the Liechtenstein Civil Code (ABGB). With this decision, the Supreme Court followed the established jurisprudence of Austria.⁵ The Austrian Supreme Court held that, in the cases of the execution of falsified orders, no action induced by the client has been taken and thus the bank does not suffer the damage by fulfilling an order given by said client. In other words, there is no sufficient link to the contractual relationship between the credit institution and its customer, to assume the applicability of the straight risk liability of Section 1014 of the ABGB. With its ruling dated 1 December 2017, the Supreme Court not only followed the Austrian jurisprudence, but was also in line with the respective jurisprudence of Switzerland⁶ and Germany.⁷

Further, the Supreme Court held that a clause in the bank's general terms and conditions, according to which the customer bears all risks of the execution of forged payment orders, is grossly disadvantageous and therefore impermissible under Section 879 of the ABGB.⁸

It should be noted at this point, that an exclusion of any liability, thus also liability for intentional damages, is not permissible according to Liechtenstein law.⁹ Whether the exclusion of gross negligence is permissible, is disputed. In general, it is stated that an exclusion for gross negligence can be agreed on, but it is immoral and thus void, if the negligence is considered to be of a certain blatancy.¹⁰ Further, it has to be taken into account that Liechtenstein has transposed Directive 2011/83/EU of 25 October 2011 on consumer rights, which is why an exclusion of liability for gross negligence is not permissible with regard to consumers. The exclusion of ordinary negligence is – with certain exceptions – permissible in Liechtenstein.

ii Banking secrecy versus data protection

In a fairly recent decision, the Liechtenstein courts dealt with the banking secrecy provided for by Article 14 of the Liechtenstein Banking Act (BA).

In this specific case,¹¹ the court had to decide if a Liechtenstein-domiciled bank is obliged to provide information regarding the existence, more specifically, the non-existence of a banking relationship with a customer, based on a request for information from a third party, referring to Article 11 of the Data Protection Act (DSG). In this regard, the court held that,

4 OGH 5 July 2013, 10 CG.2010.152, LES 2013, 156; OGH 9 February 2006, 06 CG.2004.23, LES 2006, 468.

5 ÖOGH 4 Ob 179/02f, SZ 2002, 153, ÖBA 2003, 129, RdW 2003, 66.

6 BGE 132 III 449; BGE 122 III 27; BGE 112 II 450.

7 BGH XI ZR 325/00.

8 OGH 1 December 2017, 03 CG.2016.302, LES 2018, 38.

9 *Krejci in Rummell/Lukas*, ABGB4, Section 879 Rz 123.

10 *Krejci in Rummell/Lukas*, ABGB4, Section 879 Rz 124.

11 OGH 5 February 2016, 02 NZ.2014.85, LES 2016, 50.

even though banking secrecy is not absolute,¹² it must be borne in mind that, according to a decision of the Liechtenstein Constitutional Court, banking secrecy has constitutional status despite being implemented as an ordinary law.¹³ Banking secrecy is intended to protect the privacy of a legal subject and this protection is guaranteed by the right of personal freedom set out in Article 32 of the Constitution of the Principality of Liechtenstein (LV).

Already, the mere fact that a business relationship exists between the customer and the bank is subject to banking secrecy, which is why banking secrecy may also be violated if negative information is provided. This is owing to the fact that negative information may allow the existence of such a customer relationship to be concluded (e.g., by inversion).

In this case, the Supreme Court had to assess whether, in light of the above, such negative information, meaning a confirmation of the non-existence of a relationship between a certain customer and the bank, may be provided to non-customers on the basis of the DSG. In this regard, it has to be noted that in its rulings, the Supreme Court has repeatedly emphasised that a bank is only obliged to provide information to the account holder.¹⁴ In a recent decision, the Supreme Court held, under consideration of a Constitutional Court ruling,¹⁵ that banking secrecy is to be considered a special statutory provision that takes precedence over the right to information, pursuant to Article 11 of the DSG. Information that could violate banking secrecy is under no circumstances covered by the DSG. Since this principle is also applicable to negative information, non-customers are not entitled to receive such negative information.

iii Liechtenstein banking secrecy in legal assistance

In another recent decision, the Supreme Court dealt with the persistence of banking secrecy in connection with the provision of legal assistance in criminal matters.

The Liechtenstein Code of Criminal Procedure (StPO) provides for the obligation of banks to surrender all documents and other material concerning the type and scope of the business relationship as well as business transactions and other business events related to such business relationship from a certain period of time upon court ruling to such effect, if it is necessary in the investigation of a case of money laundering, a predicate offence to money laundering or an offence in connection with organised crime.¹⁶

Where the district court ruled that a bank should surrender account statements in a mutual legal assistance case regarding the violation of the obligation to provide maintenance,¹⁷ the Supreme Court held that the bank was not obliged to surrender the account statements, since it was not ordered in connection with the investigation of a case of money laundering, a predicate offence to money laundering or an offence in connection with organised crime.

Further, the court held that where acts of investigation interfere with personal rights, legal assistance may only be granted if the conditions provided for such a measure in the StPO are met.¹⁸ Thus, there is no reason why, even in times of increasing transparency, banking

12 OGH 4 June 2009, RZ.2007.274, LES 2009, 322.

13 StGH 6 February 2006, StGH 2005/50, LES 2007, 396.

14 OGH 12 January 2006, 10 CG.2003.297, LES 2006, 388.

15 StGH 29 August 2011, StGH 2011/11, GE 2013, 66.

16 Section 98a StPO.

17 Section 197 Liechtenstein Criminal Code.

18 BuA 2000/55, 49.

secrecy in Liechtenstein should be penetrated any further in cases of mutual legal assistance in criminal matters than in domestic criminal proceedings. This decision proves that banking secrecy is of great importance to the Liechtenstein legal system.¹⁹

iv Prolongation of asset freezing orders

As asset freezing orders often concern banks, especially as third-party debtors,²⁰ the recent decision of the Supreme Court dealing with the prolongation of such an asset freezing order is also of interest here. In general, asset freezing orders, which are based on criminal law, may only be ordered for a period of a maximum of two years and may only be extended for a year each upon application after that.²¹

The Constitutional Court holds, in settled case law, that asset freezing orders interfere with the property guarantee that is provided for by Article 34 of the LV and thus, only permissible if the necessary intervention criteria, including the principle of proportionality, are complied with. According to the case law developed in this regard, a freezing of assets beyond three years is already unreasonable, unless expedient investigations are conducted or results of such are available, which confirm the initial suspicion, or special circumstances worthy of special consideration, which justify an extension beyond three years, are given.²² Thus, freezing of assets for several years does not automatically result in a breach of the property guarantee.²³

In light of the above, the Supreme Court has recently decided that, under special circumstances, an extension of an asset freezing order that has already been in place for 13 years is not an unreasonable impairment of the property guarantee protected under Article 34 of the LV or under the first supplementary protocol to the European Convention on Human Rights and does not violate the principle of proportionality.²⁴ In this particular case, the Supreme Court reasoned that the scope and complexity of the facts, the strong foreign connection and the need to await the results of foreign criminal proceedings to clarify the facts of the case, constitute such special circumstances mentioned above.

III LEGISLATION AND SUPERVISION

By virtue of its EEA membership, Liechtenstein implements EU directives with EEA relevance. In the financial services sector in particular, Liechtenstein is obliged to transpose EU directives and regulations. Thus, financial institutions in Liechtenstein are subject to the same regulatory framework as financial institutions located in EU Member States and EU law has great impact on legislation in Liechtenstein's financial centre.

Recent legislative developments in the banking sector have been the implementation of Directive 2014/65/EU of 15 May 2014 on markets in financial instruments (MiFID II) and the transposition of Directive (EU) 2015/849 of 20 May 2015 on the prevention of the use

19 OG 19 January 2016, 12 RS.2015.166, LES 2016, 76.

20 *Drittschuldner*.

21 Section 97a, Paragraph 4 StPO.

22 StGH 30 November 2009, StGH 2009/149, GE 2010, 373; OGH 2 November 2006, 12 RS 2003.202-55, LES 2007, 462; OGH 3 October 2007, 13 UR.2001.151-131, LES 2008, 191, *inter alia*.

23 OGH 6 August 2009, 12 UR.2001.39-1718, LES 2010, 63; StGH 29 October 2013, StGH 2013/93 GE 2014, 99.

24 OGH 21 July 2017, 11 UR.2003.365, GE 2018, 32.

of the financial system for the purpose of money laundering and terrorist financing, better known as the Fourth Anti-Money Laundering Directive (4th AMLD). The transposition of Directive (EU) 2015/2366 of 25 November 2015 on payment services in the internal market (PSD II) is scheduled to take place in the near future, presumably at the beginning of 2019.

In Liechtenstein, the relevant supervisory authority is the Liechtenstein Financial Market Authority (FMA), which is part of the European system of financial supervision. Even though Liechtenstein is not a member of the European Union, it is a full member of the European Banking Authority, the European Securities and Markets Authority and the European Insurance and Occupational Pensions Authority; however, the FMA has no voting rights in the committees of these financial supervisory authorities.

i MiFID II and the Regulation on markets in financial instruments

Certainly one of the major legislative developments of the recent past has been the implementation of MiFID II, which required comprehensive amendments to the BA, the Asset Management Act and the respective ordinances, as well as adjustments to the Law on specific undertakings for collective investment in transferable securities. The legislative process has been completed, and the respective amendments entered into force on 3 January 2018.

Through the implementation of MiFID II and the Regulation on markets in financial instruments (MiFIR), investor protection has been enhanced by requiring the provision of improved information to customers with regard to the services provided to them. Further, in accordance with EU law, independent investment advice and portfolio management have been introduced in conjunction with a new legal framework for fees, commissions or other monetary or non-monetary benefits received from or granted to third parties, in particular product providers.

With regard to the scope of the term ‘financial instruments’, an expansion to commodities and other derivatives, which are comparable with traditional financial instruments from a regulatory perspective, was conducted. In addition, markets for financial instruments, including over-the-counter trading, are now subject to stricter regulation, aiming for transparency and investor confidence.

In addition to the above-mentioned amendments, *inter alia*, the powers of the supervisory authorities have been enhanced and certain trading techniques, in particular the algorithmic high-frequency trading, are now subject to regulation.

However, with respect to the applicability of MiFIR, it has to be taken into account that Liechtenstein is a member of the EEA but not the European Union itself, which is why MiFIR will only be directly applicable without the need of national transposition after its incorporation into the EEA *acquis*. The transposition process has already been initiated, but at this time it is difficult to predict when the transposition will be finalised. While MiFIR has been applicable in EU Member States since 3 January 2018, it is not yet applicable in Liechtenstein.

ii PSD II

Further, the national implementation of PSD II is in progress. The main contents of this are, in particular, the extension of the scope of application to transactions with EU third countries and payments in foreign currencies, as well as increased transparency and information obligations. In addition, consumer protection and safety requirements will also be enhanced.

In the course of the implementation of PSD II, a law on payment services will be enacted and several other laws will be amended, including, *inter alia*, the BA. At this point, it is difficult to predict when the respective national implementation laws will enter into force in Liechtenstein, but the beginning of 2019 seems likely.

iii Anti-money laundering

In addition to the above-mentioned regulations, the 4th AMLD was transposed into Liechtenstein law quite recently, with the exception of the provisions regarding the requirement to establish beneficial ownership registers. In the course of the transposition, the Liechtenstein Due Diligence Act (DDA) and its respective ordinance were amended accordingly. Further, alongside the transposition of the 4th AMLD, Liechtenstein decided to address the most recent assessment regarding Liechtenstein's compliance with the Financial Action Task Force Recommendations.²⁵ The respective national implementation law entered into force on 1 September 2017.

The scope of the DDA was extended with regard to asset management companies and undertakings for collective investment and thus, aligned with the scope defined by the 4th AMLD. Further, in anticipation of the 5th AMLD, virtual currency exchanges now also fall within the scope of the DDA.

The major amendments in the national law that were made in order to comply with the provisions set out in the 4th AMLD include the adjustment of the definition of beneficial ownership regarding legal entities and arrangements, as well as the extension of the definition of a politically exposed person. Further, *inter alia*, the responsibility for the submission of suspicious transaction reports to the Liechtenstein Financial Intelligence Unit has been laid out more clearly; the threshold with respect to the obligation to conduct customer due diligence was reduced to 10,000 Swiss francs, and the DDA now stipulates the obligation to appoint a member at the executive level as responsible for the compliance with the DDA and its respective ordinances.

Regarding the supervisory framework, a stronger risk-based supervision is provided for by the revised DDA, according to which the FMA has to prepare a risk profile for subjects to due diligence. In addition, the range of supervisory measures has been extended to align with the requirements set out in the 4th AMLD, and the maximum for fines for qualified infringements has been significantly increased. Moreover, the introduction of liability of legal entities in administrative criminal proceedings and the transfer of certain offences away from the courts to the jurisdiction of the FMA has been effected.

IV PROCEDURAL ISSUES

As banks often play a key role in interim measures, especially as third-party debtors, this section focuses on interim measures in Liechtenstein.

25 Conducted by the IMF and MONEYVAL in 2013 and 2014, Report on Fourth Assessment Visit, MONEYVAL (2014).

i Civil law interim measures

General remarks

The Liechtenstein Enforcement Act (EO) provides for the possibility to request a preliminary injunction to secure either a monetary claim or any other claim before or pending a civil case or execution proceedings.²⁶ The relevant provisions concerning interim injunctions are contained in Articles 270 et seq. of the EO and have been implemented on the basis of the Austrian provisions with regard to interim measures. Consequently, the courts and legal representatives must consider Austrian legal doctrine and jurisprudence when dealing with interim injunctions.

As banks will most commonly only be affected by preliminary injunctions to secure a monetary claim, this section focuses on such. According to Article 274, Paragraph 2 of the EO, interim injunctions to secure monetary claims may be issued, if it is likely that without an interim measure, the debtor could prevent or impede the recovery of a monetary claim through acts such as damaging, destroying, concealing or side-lining assets or through the sale or other disposal of assets. Thus, an application for an interim injunction must be based on an element of subjective endangerment as set out above. Such endangerment shall in particular also be assumed, if the debtor (1) has no fixed address; (2) is making arrangements to flee or is fleeing with the intention of avoiding his or her obligations; or (3) does not reside in Liechtenstein or if the execution title would have to be enforced abroad.²⁷ The practical significance of the enforcement of the execution title abroad as a reason for endangerment represents a peculiarity of Liechtenstein law and a distinction from the Austrian legal situation. This is owing to the fact that Liechtenstein is not a member of the European Union and thus, Liechtenstein execution titles will not automatically be enforced in EU Member States.

Since banks will more commonly be third-party debtors than claimants, or even less commonly, debtors, the third-party prohibition as a security measure is of special interest. The court may issue a third-party prohibition if the debtor has a monetary claim or any other claim for performance or delivery of any item.

Such a third-party prohibition is enforced by prohibiting the debtor from disposing of the claim and ordering the third party not to pay the debt owed to the debtor and not to undertake anything in relation to the debtor that could impede or prevent the recovery of the respective claim.²⁸ In contrast to the legal situation in Austria, in Liechtenstein, the creditor will acquire a lien on the secured claims.²⁹ Thus, the bank will be prohibited from disposing of the claim for repayment that the debtor has acquired against it and the creditor will have a lien in said claim.

Procedure

Regarding the filing of an application of an interim injunction, which may be done separately or in conjunction with a claim, application for a payment order or any other application, certain details must be provided, *inter alia*, the type of order the applicant wishes to apply for and its proposed duration. Further, the creditor's claim must be specified precisely and the facts on which the request is based must be stated truthfully and in detail.

26 Article 270, Paragraph 1 EO.

27 Article 274, Paragraph 3 EO.

28 Article 275, Paragraph 2 EO.

29 OGH 4 April 2002, 09 CG.165/2000-38, LES 2003, 29.

Against the issuing of an interim injunction, the debtor has the right to appeal within 14 days upon receipt of the interim injunction.³⁰

Since the procedure regarding interim injunctions, the purpose of which is to prevent the enforcement of a securable claim from being frustrated, is an urgent and summary one, numerous procedural peculiarities take this, and the endeavour to complete the procedure quickly, into account.³¹

Cross-border interim measures

Since Liechtenstein is not part of the European Union, it cannot be assumed that foreign interim measures will automatically be enforced in Liechtenstein and vice versa. Regarding detailed information on jurisdictional matters, see Section VI, below.

ii Asset freezing orders based in criminal law matters

Since asset freezing orders are not only issued in connection with civil law matters, asset freezing orders in criminal law should also be dealt with.

In criminal proceedings, the court must issue certain orders, including asset freezing orders, at the request of the Public Prosecutor's Office, to protect the forfeiture pursuant to Section 20 of the Liechtenstein Criminal Code (StGB) or the extended forfeiture pursuant to Section 20b of the StGB if it is to be feared that the collection would otherwise be endangered or considerably impeded. Such an asset freezing order will lead to the state acquiring a lien with regard to credit balances or other assets.³²

Further, such an order shall not be issued for a period exceeding two years and the validity period may only be extended by a maximum of one year each, upon application, as discussed in Section II.iv, above. An asset freezing order shall be lifted as soon as the circumstances under which it has been issued have lapsed.³³

V PRIVILEGE AND DISCLOSURE

The Liechtenstein Lawyers Act (RAG) provides for lawyer–client privilege in Article 15, which stipulates that lawyers are obliged to maintain secrecy about all matters entrusted to them and facts that become known to them in their professional capacity, the secrecy of which is in the interest of the lawyer's party. The lawyer–client privilege is also valid with regard to courts or other authorities since the law provides that lawyers have the right to non-disclosure in court and in other official proceedings in accordance with the respective procedural regulations.

According to the Constitutional Court, the identity of the client also falls within the scope of protection of the lawyer–client privilege. The lawyer's right to refuse testimony coincides with the professional duty of confidentiality and covers all information that a lawyer receives in his or her capacity within the framework of the client relationship. Similar to banking secrecy, lawyer–client privilege primarily serves to protect the client's personality.³⁴

Further, Article 15, Paragraph 2 of the RAG stipulates that the right of a lawyer to secrecy may not be circumvented by judicial or other official measures, in particular by questioning

30 Article 43; Article 290 EO.

31 OGH 2 December 2004, 01 CG.2002.310-108, LES 2006, 46.

32 Section 97a, Paragraph 1 StPO.

33 Section 97a, Paragraphs 4 and 5 StPO.

34 StGH 30 June 2008, StGH 2007/130, LES 2009, 6.

assistants or ordering the surrender of documents, video, audio or other data media or the confiscation of such. Lawyer–client privilege also extends to correspondence between a lawyer and the party, irrespective of where and in whose custody such correspondence may be located.

VI JURISDICTIONAL MATTERS

As a general remark, it should be noted that judgments rendered by a foreign competent court are not automatically enforceable in Liechtenstein. A court in Liechtenstein would only enforce judgments of foreign courts if enforcement is granted by respective treaties or by mutual agreement according to Article 52 of the EO. Further, enforcement of a decision of a foreign court or other authority may only be granted if certain essential principles of Liechtenstein law are met (e.g., *inter alia*, regarding the competence of the court, the service of court documents and finality of the judgment).³⁵

As Liechtenstein is not a member of the European Union, the Brussels Regulation does not apply. Liechtenstein is also not a contracting party to other international agreements on the recognition and enforcement of foreign decisions of ordinary courts. Bilateral agreements exist with Austria and Switzerland only, which ensure the acknowledged enforceability of Austrian and Swiss judgments.³⁶

With regard to other foreign judgments, irrespective of whether they were issued in the European Union or a third-country state, no treaty regarding the enforcement of foreign judgments or a mutual promise exists. Therefore, judgments rendered by foreign courts will not automatically be enforced in Liechtenstein. However, the plaintiff can apply for recognition of the judgment and the issuance of a payment order with the Liechtenstein court. Nevertheless, if the defendant opposes such an application, recognition of the foreign judgment could be refused. In such cases, new proceedings on the merits would have to be initiated in Liechtenstein.

In conclusion, any final judgment obtained against a Liechtenstein counterparty in a foreign court – except Austrian and Swiss courts – will not be automatically recognised and enforced by the courts in Liechtenstein without potential re-examination or re-litigation of the matters adjudicated.

Owing to this particularity of Liechtenstein, its accession to the New York Convention of 1958 on the recognition and enforcement of foreign arbitral awards on 7 July 2011, which entered into force in Liechtenstein on 5 October 2011, is of utmost significance. On the basis of the New York Convention, the recognition of foreign arbitral awards is granted and thus, the enforcement of a foreign arbitral award in Liechtenstein is possible, in accordance with the Convention. In light of the above-mentioned difficulties regarding foreign court judgments and Liechtenstein's accession to the Convention, an arbitration clause could be advisable. Arbitration clauses in contracts executed by both parties are binding when the requirements set out by law are complied with (i.e., the prerequisite that the arbitration

35 Article 53 EO.

36 Agreement of 25 April 1968 between the Principality of Liechtenstein and the Swiss Confederation on the recognition and enforcement of judgments and arbitration awards in civil matters; Agreement of 5 July 1973 between the Principality of Liechtenstein and the Republic of Austria on the recognition and enforcement of judgments, arbitral awards, settlements and public documents.

clause is in writing). Further, it has to display the intention of the parties to submit all or specific disputes related to a legal (contractual) relationship under the competence of an arbitral tribunal.

Also, with regard to the applicable law and international jurisdiction, it has to be borne in mind that Liechtenstein is not a member of the EU and thus, neither part of the Brussels Ia Regulation nor the Rome I Regulation, which is why international jurisdiction, as well as conflict of law issues, are determined by national law, in particular by the Act on International Private Law (IPRG) and the Court Jurisdiction Act.

Regarding banking relationships, Article 42 of the IPRG stipulates that these are determined by the law of the country in which the undertaking conducting business under the BA has its domicile³⁷ and, in the case of banking transactions between such undertakings, by the law of the domicile of the commissioned undertaking.

VII FREQUENT CAUSES OF ACTION

As outlined above, banks in Liechtenstein rarely initiate proceedings themselves but are most commonly the addressees of litigation. In the past few years, lawsuits dealing with the liability of a bank and its bodies for losses in client assets deposited with them and asset freezing orders and their prolongation, as well as the extent of banking secrecy, have prevailed in banking litigation in Liechtenstein. In addition, the enforcement of pledges in client assets has also been dealt with recently by Liechtenstein courts.

However, as mentioned above, not only the jurisprudence of the Liechtenstein courts is of importance concerning banking litigation, but Austrian and Swiss case law also influences jurisprudence in Liechtenstein and, therefore, must be taken into account.

VIII OUTLOOK AND CONCLUSIONS

Liechtenstein offers stability and security as a financial centre and financial intermediaries, such as banks, located in the Principality benefit from privileged access to the European Union and Switzerland, owing to Liechtenstein's EEA membership and its close ties to Switzerland.

The applicable regulatory framework is similar to that of EU Member States', since Liechtenstein transposes most EU law regarding the financial sector. Liechtenstein has already transposed the respective EU provisions on anti-money laundering as well as MiFID II. In the near future, PSD II will also be transposed into Liechtenstein law.

Further, Liechtenstein law provides for very strict banking secrecy, as well as attorney-client privilege, both of which are recognised by courts and other authorities. Finally, Liechtenstein is not part of any multilateral treaties addressing conflict of law issues, international jurisdiction and the enforceability of foreign judgments, which is why the enforceability of foreign judgments in Liechtenstein can be somewhat difficult.

By virtue of Liechtenstein being one of the most stable financial centres in Europe, with its banks having a core capital ratio averaging over 21 per cent and thus being among the best-capitalised banks worldwide, banking litigation is not as significant a topic as might be imagined. At the present time, it cannot be anticipated how the number of banking litigation cases filed with Liechtenstein courts might develop; however, a significant increase is not expected.

37 According to Article 40, Sentence 2 IPRG.

PORTUGAL

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I SIGNIFICANT RECENT CASES

The 2007–2008 financial crisis and the European debt crisis both had a substantial impact on the Portuguese economy and the consequences of it are still being felt, particularly in the financial system. These crises also had a decisive influence on setting the trend of the banking disputes that have been pending in the Portuguese courts ever since. The following three groups of cases have set the trend for banking litigation in Portugal in recent years: (1) disputes related to swap agreements executed between banks and state-owned companies or private entities; (2) disputes related to the amendment of finance agreements; (3) disputes related to the mis-selling of investment products by banks; and, more recently, (4) disputes to waive the banking privilege.

i Swap agreements

Disputes related to the validity of swap agreements, in particular interest rate swap agreements, have been in the spotlight in Portugal in recent years. The media focused on this controversial issue because of the large sums involved in swap agreements entered into by several banks and state-owned companies before the 2008 crisis, who faced significant pressure from the beginning of 2009 onwards when the Euribor rate fell to unprecedented values, bringing the mark-to-market of those contracts to a value that was highly unfavourable to investors and banks' clients.

Among the disputes related to swap agreements brought before the courts, three arguments can be distinguished that are invoked by the counterparties of the banks to challenge the validity of swap agreements.

First, swap agreements have been challenged by several parties based on the theory of the unexpected change in the circumstances during the negotiation of the agreement, as per Article 437 of the Civil Code.² The Supreme Court deemed this argument valid in one case, annulling the relevant swap agreement, in a decision of 10 October 2013.³ This argument

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2 Article 437, Paragraph 1 of the Portuguese Civil Code states that, 'If the circumstances on which the parties based their decision to contract change unexpectedly, the injured party has the right to terminate the contract, or to alter it according to fair judgement, as long as the requirement of the obligations which it assumed seriously affects the principles of good faith and is not covered by the actual risks inherent in the contract.'

3 Decision of the Supreme Court of Justice of 10 October 2013 (proceedings No. 1387/11.5TBCL.G1.S1).

was also deemed valid on two occasions by the courts of appeal (second instance courts).⁴ These decisions considered that the drastic fall in interest rates after the financial crisis led to huge losses for the counterparties of the banks, causing an imbalance between the parties of the swap agreement that were not covered by the normal risks of this type of agreement. Thus, owing to such an unexpected and unreasonable change of circumstances, the Supreme Court considered that the provision of Article 437 of the Civil Code was fulfilled, allowing the aggrieved party to terminate the swap agreement.

However, since the beginning of 2015, the courts of appeal, notably the Lisbon Court of Appeal,⁵ have repeatedly considered that the fall in interest rates after the financial crisis should not be deemed an unexpected change of the circumstances under the legal regime set out in Article 437 of the Civil Code. This understanding has also been confirmed by the Supreme Court⁶ upholding the validity of the swap agreements at stake.

Secondly, some swap agreements have also been challenged on the ground of their alleged speculative nature. In this context, the counterparties of the banks invoked two different causes of nullity of the swap agreements: (1) the violation of public policy, which renders the agreement null under Article 280 of the Civil Code; and (2) the qualification of swap agreements as gaming and wagering agreements, which are considered null and void under Portuguese law.

The Supreme Court, in a decision of January 2015,⁷ considered that the agreements with a purely speculative nature (i.e., that do not cover any real risks) breach public policy and are therefore null under Article 280 of the Civil Code. In a previous decision of March 2013,⁸ the Lisbon Court of Appeal had considered that the risk covered by a swap agreement must be connected to one or several parallel financial transactions, otherwise it should be considered as a wagering agreement, which is null under Article 1245 of the Civil Code. However, subsequently, the Oporto Appeal Court, in a decision of October 2015,⁹ and the Supreme Court, in decisions of February 2015 and May 2016,¹⁰ have decided in the opposite direction and accepted that Portuguese law allows for agreements with an abstract nature (i.e., the swap agreements are valid and enforceable even if not connected to parallel financial transactions, being clearly and expressly considered in those decisions that the swap agreement does not violate public policy or constitute a wagering agreement).¹¹

4 Decision of the Guimarães Court of Appeal of 31 January 2013 (proceedings No. 1387/11.5TBBCL.G1); decision of the Lisbon Court of Appeal of 8 May 2014 (proceedings No. 531/11.7TVLSB.L1-8).

5 Namely, the decisions of the Lisbon Court of Appeal of 15 January 2015 (proceedings No. 876/12.9TVLSB.L1-6), 2 July 2015 (proceedings No. 2118-10.2TVLSB.L1.-2) and 10 May 2016 (proceedings No. 1246/14.0T8PDL.L1-7).

6 Decisions of the Supreme Court of Justice of 26 January 2016 (proceedings No. 876/12.9TVLSB.L1.S1), 22 June 2017 (proceedings No. 540/11.6TVLSB.L2.S1) and 8 June 2017 (proceedings No. 2118/10.2TVLSB.L1.S1).

7 Decision of the Supreme Court of Justice of 29 January 2015 (proceedings No. 531/11.7TVLSB.L1.S1).

8 Decision of the Lisbon Court of Appeal of 21 March 2013 (proceedings No. 2587/10.0 TVLSB.L1-6).

9 Decision of the Oporto Court of Appeal of 28 October 2015 (proceedings No. 27/14.5TVPRT.P1).

10 Decisions of the Supreme Court of Justice of 11 February 2015 (proceedings No. 309/11.8TVLSB.L1.S1) and 3 May 2016 (proceedings No. 27/14.5TVPRT.P1.S1).

11 Decision of the Supreme Court of Justice of 22 June 2017 (proceedings No. 540/11.6TVLSB.L2.S1)

Thirdly, the nullity of the swap agreements has also been invoked before the courts based on error *in negotio*, and the invalidity of standard form agreements based on the lack of information that should be provided by the banks and other financial institutions under the legal regime of general contractual terms. However, this argument has not been generally upheld by superior courts.¹² Nevertheless, in a very recent case,¹³ the Supreme Court decided that there was a breach of the information duties under the legal regime of general contractual clauses, and considered that the client was not properly informed of the precise terms of the swap or the associated risks.

The validity of the jurisdiction clauses contained in swap agreements has also been discussed before the Portuguese courts – see Section V, below.

ii Amendment of finance agreements

In recent years, there was some litigation before the Portuguese courts about the amendment of finance agreements. Several debtors have filed lawsuits against the banks in which it has been argued that the financial crisis should be considered as an unexpected change in the circumstances considered during the negotiation of the agreement, which, in turn, would require the amendment of such agreements.

However, Portuguese courts have generally rejected the consideration of the financial crisis as an unexpected change in circumstances and therefore dismissed this kind of claim.¹⁴

iii Disputes related to the mis-selling of investment products by banks

The number of disputes related to the breach of duties attributed to financial intermediaries also increased in Portugal because of the financial crisis. In fact, the market turmoil affected several investment products sold by banks to clients, which, in turn, raised questions about the role of banks acting as financial intermediaries.

In this context, numerous mis-selling claims have been started by clients against banks in the past few years and have, since then, been judged. In particular, the focus has been on the adequacy and completeness of the information provided by banks to clients. The approach of Portuguese courts to these cases has evolved over time.

Initially, Portuguese courts tended to be protective of clients, particularly when the investment product originated from entities that had some kind of relationship with the bank (which acted as a financial intermediary). In some cases, the courts have found the banks liable for damage caused to clients by investment products that were sold several years before the financial crisis, and that have only become problematic as a result of the crisis. This was

12 Decisions of the Lisbon Court of Appeal of 2 July 2015 (proceedings No. 2118-10.2TVLSB.L1.-2) and 27 September 2016 (proceedings No. 1961/13.5TVLSB.L1-1); decisions of the Supreme Court of Justice of 16 June 2015 (proceedings No. 1880/10.7TVLSB.L1.S1) and 8 June 2017 (proceedings No. 2118/10.2TVLSB.L1.S1); and decision of the Guimarães Court of Appeal of 25 January 2018 (proceedings No. 1122/14.6TBBRG.G1).

13 Decision of the Supreme Court of Justice of 4 April 2017 (proceedings No. 1961/13.5TVLSB.L1.S1).

14 Decisions of the Supreme Court of Justice of 10 January 2013 (proceedings No. 187/10.4TVLSB.L2.S1) and 27 January 2015 (proceedings No. 876/12.9TBBNV-A.L1.S1) and decision of Oporto Court of Appeal of 6 June 2016 (proceedings No. 4463/14.9TBVNG-A.P1).

the case in the Supreme Court decision of 10 January 2013,¹⁵ in which a bank was held liable for damages caused to a client by a debt security sold in 2001, at a time when the financial crisis was not expected.¹⁶

Portuguese courts have typically been keen to protect individual investors, notably when banks have breached their duty to provide investors with adequate and complete information about the products sold.

Nevertheless, in some cases the courts have used a more thorough analysis. For instance, in the decision of the Lisbon Court of Appeal of 28 April 2016,¹⁷ the court analysed a case in which the bank had informed a client that the bonds issued by an Icelandic bank and a Greek bank, which were later bailed out, were safe investments with guaranteed capital returns. The court decided that there was no mis-selling by the financial intermediary, as the market perception about the bonds in question before the financial crisis was that they were safe products, similar to bank deposits. Therefore, considering that the financial crisis was not likely to be anticipated at that time, the court understood that the information provided by the bank to the client was appropriate and adequate. In another case, the Coimbra Court of Appeal¹⁸ decided that the conduct of a bank that presented to a client (with a conservative risk profile, without knowledge or experience of the securities market), as a risk-free product, the bonds issued by Icelandic banks that at that time had positive investment grade ratings by Moody's and Fitch, with Iceland sovereign bonds having an identical rating, was not unlawful.¹⁹

In any case, in the majority of the cases, the courts have been holding the financial intermediaries liable for the repayment of principal and interest payable under the same terms on which the issuers would be, if proved that the decision to subscribe to the financial product was based on misleading information provided by financial intermediaries' officials regarding the financial product in question (e.g., no or low risk, lack of clarification on the characteristics of the financial product, aggressive sales techniques, etc.).²⁰

Take, for instance, the most recent judgment on the matter – the decision of the Lisbon Court of Appeal of 22 February 2018.²¹ In this case, a bank's official persuaded an individual client²² to invest his savings (in the amount of €100,000) in junior bonds, comparing their

15 Proceedings No. 89/10.4TVPRT.P1.S1.

16 This decision prompted an important dissenting opinion statement by one of the judges (Counselling Judge Abrantes Geraldés) that was followed with other decisions of the Supreme Court and Courts of Appeal. According to this statement, the decision of the Supreme Court was wrong because, among other reasons, it did not establish a sufficient connection between the breach by the bank of its financial intermediary duties and the damages caused by the investment product as a consequence of the financial crisis.

17 Proceedings No. 428-12.3TCFUN.L1-6.

18 Decision of the Coimbra Court of Appeal of 15 December 2016 (proceedings No. 377/12.5TVPRT.C2).

19 This kind of discussion will continue, especially as a result of the financial crisis that led to the application of the resolution measure to Banco Espírito Santo in August 2014.

20 Decision of the Oporto Court of Appeal of 30 May 2017 (proceedings No. 588/11.0TVPRT.P1) and decision of the Coimbra Court of Appeal of 16 January 2018 (proceedings No. 3906/10.1T8VIS.C1).

21 Proceedings No. 20742/16.

22 The court emphasised the fact that the bank's official knew that the client possessed no particular qualification to understand the various forms of financial products was relevant.

risk to that of a regular term deposit. By failing to provide the due gains to the client, the bank was held liable to repay the client the due principal amount applied, as well as interest accrued and guaranteed (€115,000).

The relevance that the resolution measures have assumed should also be noted – see Section II, below – in the context of these disputes. In fact, many proceedings have been recently decided (and terminated) by taking into account the effects of these regulatory acts of the Bank of Portugal (BOP), namely the power to establish the ‘perimeter’ among assets and liabilities to be transferred (or not) from the ‘bad bank’ to the ‘good bank’. This has been shown to be a very contentious issue, considering the impact that the non-transfer of a mis-selling liability poses to investors.

See the following decisions, for example:

- a Lisbon Court of Appeal of 11 May 2017,²³ according to which the applicants pleaded for contractual liability based on the breach by the ‘bad bank’ of its duties to inform and act loyally, alleging that they were informed that their investment corresponded to a term deposit, when, in fact, they were acquiring shares on a special purpose vehicle from Jersey;
- b Lisbon Court of Appeal of 11 May 2017,²⁴ in which the applicant alleged that it ended up investing in preferential shares, instead of a term deposit, as pretended; and
- c Lisbon Court of Appeal of 7 March 2017,²⁵ in which the applicants alleged that they were pressured to acquire a financial product, the details of which were not disclosed to them.

In all of the above-mentioned judgments, the court established that the referred liability had not been transferred to the ‘good bank’, based on a harmonised set of arguments: (1) the BOP holds the necessary legal powers to determine the transfer of all the assets and liabilities from the ‘bad bank’ to the ‘good bank’; (2) the analysis of the lawfulness of the transfer falls within the jurisdiction of the administrative courts; and (3) the legal regime of bank resolution, especially the scope of the transmission process, is not subject to any unconstitutionality.²⁶

II RECENT LEGISLATIVE DEVELOPMENTS

It comes as no surprise that the most significant recent legislative development in the field of banking law should be the implementation of the widely acknowledged Banking Recovery and Resolution Directive (Directive 2014/59/EU of the European Parliament and of the Council of 14 May) (BRRD). The implementation of the BRRD in Portugal was not a straightforward process. The first step towards the establishment of a national banking resolution framework took place in 2012 prior to the publication of the BRRD, as part of the 2011 financial assistance programme entered into with the European Commission, the

23 Proceedings No. 31411/15.6T8LSB.L1-8.

24 Proceedings No. 2471/16.4T8LSB-2.

25 Proceedings No. 48/16.3T8LSB-L1-7.

26 The resolution measures have, thus, been challenged on several grounds, namely based on several rights foreseen in the Portuguese Constitution (CRP): (1) ownership rights under Article 62 of the CRP; (2) principle of equality, under Article 13 of the CRP; (3) principle of proportionality; and (4) confidence protection, among others – all of which have been continuously rejected by the high courts.

European Central Bank and the International Monetary Fund.²⁷ Two years later, in 2014, the government approved legislation implementing the BRRD a mere two days before the announcement of the resolution of Banco Espírito Santo (BES), one of the largest private banks in Portugal at the time. Full implementation of the BRRD followed in 2015.²⁸

The BRRD was implemented mainly by amending the General Regime for Credit Institutions and Financial Companies (Decree-Law No. 298/92 of 31 December 1992) (RGICSF). The resolution mechanisms foreseen in the RGICSF and the conditions for their application are mostly in line with those established in the BRRD. The BOP, as the resolution authority, can apply a resolution measure provided that the following conditions are met:

- a* it has determined that the institution is at risk of, or in a situation of, insolvency (termed ‘failing or likely to fail’ in the BRRD);
- b* resource to alternative measures is not a viable option;
- c* the measure is necessary and proportional with a view to achieving the resolution objectives;²⁹ and
- d* the winding up of the institution would not have achieved those objectives more successfully.³⁰

The resolution tools set out in the RGICSF, as foreseen in the BRRD, are: (1) the sale of business tool; (2) the bridge institution tool; (3) the asset separation tool; and (4) the bail-in tool. Thus far, the bridge institution tool has been applied to BES, and the sale of business and asset separation tools to Banco Internacional do Funchal (Banif), a Portuguese bank to which a resolution measure was applied in December 2015.

One of the most relevant aspects as far as banking litigation is concerned, especially in Portugal and the BES resolution, is the separation of assets, rights and liabilities between the ‘bad bank’ and the ‘good bank’. According to the RGICSF, the BOP will select the assets, liabilities, off-balance sheet items and assets under management to be transferred from the bank under resolution to the bridge bank, which is a discretionary power (and includes the power to retransfer to the bank under resolution such assets³¹), subject to two main limitations. First, the total value of the liabilities transferred to the bridge institution cannot exceed that of the transferred rights.³² Second, pursuant to the RGICSF, the rights held by shareholders who owned more than 2 per cent of the bank’s share capital in the two-year period preceding the resolution, and held by members of the bank’s administration and supervision bodies, cannot be transferred to the bridge bank.³³

In the wake of the BES resolution, the breach of the principle of equality of creditors is being invoked as a ground for challenging the resolution mechanism applied to BES before

27 See MOU available on http://ec.europa.eu/economy_finance/eu_borrower/mou/2011-05-18-mou-portugal_en.pdf, p. 7 and Decree-Law No. 31-A/2012 of 31 March 2012.

28 Decree-Laws Nos. 114-A/2014 of 1 August 2014 and 114-B/2014 of 4 August 2014; and Law No. 23-A/2015 of 31 March 2015.

29 Such objectives are, pursuant to Article 145-C of the RGICSF, to ensure continuity of essential financial services; to avoid serious adverse effects on financial stability; to protect taxpayers and public funds; to protect depositors covered by Directive 2014/49/EU and investors covered by Directive 97/9/EC; and to protect client funds and client assets held by financial institutions.

30 Article 145-E, Paragraphs 2 and 145-C RGICSF.

31 Article 145-Q, Paragraph 4, sub-paragraph c) RGICSF.

32 Article 145-Q, Paragraph 7 RGICSF.

33 Article 145-Q, Paragraph 3 RGICSF.

the courts, notably as shareholders and junior creditors were left in the ‘bad bank’.³⁴ There has been also litigation connected with the BOP’s decision taken in December 2015 to transfer to BES senior bonds worth €2 billion³⁵ and to ‘leave behind’ an €835 million liability arising from a facility agreement.^{36,37}

Notwithstanding the asset separation, following the application of any resolution measure under the RGICSF no creditor or stakeholder can incur greater losses than those he or she would have incurred had the bank been wound up (the ‘no creditor worse off’ principle³⁸). This is ensured through (1) carrying out an independent evaluation of the total value of the assets of the bank prior to the application of the resolution measure; and (2) the right to be compensated by the resolution fund for the losses, should the evaluation demonstrate a breach of the principle.³⁹

Finally, the Portuguese banking resolution regime contains a specific provision governing the right of appeal of resolution decisions, which is aligned with Article 85, No. 3 of the BRRD. This provision specifies that the decisions of the BOP that apply resolution mechanisms, exercise resolution powers or appoint board members can be challenged under the general administrative procedural rules.⁴⁰ It further states that if a ruling⁴¹ declares that a BOP decision is void, the BOP can oppose the enforcement of such ruling, following which compensation will be due to those affected by ruling not being enforced. As mentioned above, several actions were started before Portuguese administrative courts seeking the annulment of the BES resolution decision, but it may take some years before a decision is made.

Also noteworthy was the issuance of Decree-Law No. 74-A/2017 of 23 June 2017 on the credit contracts relating to immovable property, establishing the rules applicable to consumer credit when secured by mortgage or other rights over immovable property – which partially implements Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014. The law, which entered into force on 1 January 2018, foresees a set of rules concerning credit agreements, focusing on the protection of consumer rights and personal guarantors and thus foreseeing a set of duties encumbered on the creditor (duty to assist the consumer, under Article 14; duties to evaluate the debtor’s solvency, and the immovable properties’ value, under Article 16 et seq.; and the duty to adhere to alternative dispute resolution mechanisms). The breach of the provisions of the referred Decree-Law by creditors is punishable with fines amounting from €1,000 to €1.5 million.

Directive 2014/17/EU became fully implemented with Decree-Law No. 81-C/2017 of 7 July 2017 on the credit intermediary activity and the provision of advisory services

34 See <http://observador.pt/2014/11/04/tribunal-ja-tem-tres-pedidos-para-anular-divisao-bes-em-fois>.

35 See the BOP’s resolution available on www.bportugal.pt/en-US/OBancoeoEurosistema/Esclarecimentospublicos/Documents/Deliberation20151229_retransfer.pdf and www.publico.pt/2017/04/03/economia/noticia/blackrock-quer-impugnar-venda-do-novo-banco-1767553.

36 See the BOP’s resolution available on www.bportugal.pt/en-US/OBancoeoEurosistema/Esclarecimentospublicos/Documents/Deliberation20151229_Perimeter.pdf and www.jornaldenegocios.pt/empresas/banca---financas/detalhe/grupo_de_investidores_da_oak_intenta_accao_contra_novo_banco_nos_tribunais_ingleses.

37 Although not focused on as much by the media, litigation has also been commenced on the same issues in relation to the resolution measure applied to Banif.

38 Article 145-D, Paragraph 1, sub-paragraph c) RGICSF.

39 Article 145-H RGICSF.

40 Article 145-AR RGICSF.

41 Article 145-AR, Paragraph 3 RGICSF.

in relation to credit agreements concluded with consumers. The Decree-Law establishes the need for intermediaries to apply for authorisation to perform their activity, under Article 11 et seq.; and technical and reputational requirements to perform their activity, under Articles 12, 13 and 14; among other provisions regulating the intermediary and consultancy activities. The breach of the provisions of the referred Decree-Law by creditors is punishable with fines amounting from €750 to €250,000.

Lastly, the approval of a series of new laws regarding information duties and compliance of the financial institutions should also be noted, namely: (1) Law No. 83/2017 of 18 August 2017, which establishes measures on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, implementing the widely acknowledged Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015; (2) Law No. 89/2017 of 18 August 2017 on the beneficial owner regime and registry, implementing Chapter III of Directive (EU) 2015/849; (3) Law No. 30/2017 of 30 May 2017, on the freezing and confiscation of instrumentalities and proceeds of crime in the implementing Directive 2014/42/EU of the European Parliament and of the Council of 3 April 2014; and (4) Law No. 109/2017 of 24 November 2017, implementing the 45th amendment to the RGICSF on conflicts of interests and reputation.

III INTERIM MEASURES

The Code of Civil Procedure sets forth a wide range of interim relief measures in order to ensure the effectiveness of the final decision adopted by the court. In general, the court may order an interim relief measure if a party suffers serious damage that is the result of a threat to the effectiveness of its rights, and that is difficult to repair.

Interim relief measures may be statutory or non-statutory. Statutory measures are specified in the Code of Civil Procedure – for example, freezing orders, provisional restoration of the possession of assets and suspension of corporate bodies' decisions. Non-statutory measures may consist of any type of measure aimed at securing the effectiveness of the affected right.

In order to apply for an interim relief measure, a party must submit a request to the court either in the course of an ongoing judicial lawsuit or in advance of commencing the main proceedings. The interim relief measure is therefore generally linked to main proceedings. According to the Civil Procedure Code, the court may, under certain circumstances, turn the interim relief measure into a final decision, in which case the defendant will have the burden of initiating a new lawsuit in order to challenge said measure.

Under the Portuguese general civil regime, the judicial seizure of an asset depends, in principle, on proof by the creditor of the just fear of loss of its patrimonial guarantee. However, under the Portuguese legal framework of financial leasing,⁴² a special regime is foreseen, where the lessor is entitled to request the court to provide a protective measure consisting in the immediate and direct delivery of the leased asset to the lessor, in cases where, after the term of the lease agreement or its breach, the lessee does not proceed with the voluntary restitution of the asset to the lessor. In these situations, the financial lessor must

42 Decree-Law No. 149/95 of 24 June 1995, as amended.

previously request the cancellation of the lease registration, and, in the request addressed to the court, provide brief evidence of the term or breach of the lease agreement and of the situation of non-restitution of the asset.⁴³

On 18 January 2017, Regulation (EU) No. 655/2014 of the European Parliament and of the Council of 15 May 2014 (the Regulation) entered into force establishing a European Account Preservation Order (EAPO) procedure to facilitate cross-border debt recovery in civil and commercial matters. The Regulation creates a European procedure as an alternative to national procedures, which will only be applicable in cross-border cases. This procedure enables a creditor to obtain an EAPO that prevents the subsequent enforcement of the creditor's claim from being jeopardised through the transfer or withdrawal of funds up to the amount specified in the EAPO that are held by the debtor or on his or her behalf in a bank account maintained in a Member State.

In order to obtain an EAPO, the creditor has to submit sufficient evidence to satisfy the court that there is an urgent need for a protective measure in the form of a preservation order because there is a real risk that, without such a measure, the subsequent enforcement of the creditor's claim against the debtor will be impeded or made substantially more difficult. Where the creditor has not yet obtained a judgment in a Member State, or court settlement or an authentic instrument requiring the debtor to pay the creditor's claim, the creditor shall also submit sufficient evidence to satisfy the court that he or she is likely to succeed on the substance of his or her claim against the debtor.

This is an *ex parte* procedure, which means that the debtor shall not be notified of the application for a preservation order or be heard prior to the issuing of the order. Before issuing a preservation order in a case where the creditor has not yet obtained a judgment, court settlement or authentic instrument, the court shall require the creditor to provide security for an amount sufficient to prevent abuse of the procedure and to ensure compensation for any damage suffered by the debtor as a result of the order to the extent that the creditor is liable for such damage (by way of exception, the court may dispense with the provision of security if it considers it inappropriate in the circumstances of the case).

Where the creditor has already obtained an enforceable judgment, court settlement or authentic instrument, the creditor may ask for information on whether the debtor holds one or more accounts in a specific Member State before a preservation order is issued, from the designated information authority of the Member State in which the creditor believes that the debtor holds an account.

Banks have an obligation to declare whether and to what extent the order has led to the preservation of any funds of the debtor. Creditors have an obligation to ensure the release of any funds preserved that exceed the amount specified in the order.

IV LAWYER–CLIENT PRIVILEGE

With regard to attorney–client privilege, confidentiality must be maintained in respect of facts of which a lawyer (a member of the Portuguese Bar Association) becomes aware during the

43 A similar regime is applicable, under the terms of the Code of Civil Procedure, where the purchase price of an asset is due in full or in part. In these cases, the creditor can obtain the judicial seizure of the asset, without having to prove the just fear of loss of its patrimonial guarantee. However, in these situations, the asset stays under judicial protection and is not delivered directly to the creditor, as is the case in the financial leasing regime.

course and as a result of the practice of his or her legal profession, pursuant to the Portuguese Bar Association Professional Conduct Rules. The determining factor is not whether a certain document is in itself privileged, but that lawyers in Portugal are under a duty not to disclose confidential information.

In addition, this privilege is non-waivable by the client, meaning that, even if the client releases the lawyer from the privilege obligations, the lawyer will still be bound to those obligations.

The form of the information does not matter – as long as the information itself is privileged, the ‘document’ will be privileged. However, a lawyer in Portugal may disclose privileged information to the extent that it is absolutely necessary to preserve the lawyer’s or the client’s reputation, legal rights and legitimate interests, and provided that prior authorisation is obtained from the relevant entities of the Bar Association.

Information disclosed in the context of a dispute in contravention to attorney–client privilege rules cannot be taken into consideration by the courts for the purposes of issuing a final decision.

Privilege, as set out by Portuguese law, applies to all lawyers registered with the Portuguese Bar Association in the practice of their profession, both in Portugal and abroad. Likewise, the aforementioned rules also apply to EU lawyers who practise their profession in Portuguese territory, as long as they are members of a foreign bar association.

Foreign lawyers exercising their profession in foreign territories are not bound by Portuguese law provisions on privilege. However, if a document is produced by a foreign lawyer in a foreign territory at the request of a Portuguese lawyer, Portuguese provisions on privilege will apply. The doctrine of privilege is respected and applied in Portugal. However, where a judge wants a lawyer to testify in criminal proceedings, the Portuguese Bar Association must present a written opinion beforehand regarding privilege issues. In relation to criminal and other investigations carried out by regulatory authorities, the investigative bodies generally require judicial authorisation before searching premises and seizing documents. When the search is carried out in a lawyer’s office, it must be led by the judge, and the presence of a Portuguese Bar Association member is always required. They may interview lawyers and request disclosure of information or documents relevant to the inquiry.

A breach of attorney–client privilege is a very serious offence. Not only can it constitute grounds for a lawyer to be disbarred from the Portuguese Bar Association, which would mean being prohibited from practising in Portugal, but it can also give rise to criminal charges.

V JURISDICTION AND CONFLICTS OF LAW

The issue related to the validity of the jurisdiction clauses and choice of law – usually English jurisdiction and English law – in swap agreements was one of the most disputed and publicised issues brought before the Portuguese courts recently.

Most of the swaps agreements entered into with state-owned companies, and some of those entered into by private parties, were subject to English law and jurisdiction – normally because of the fact that they were made with reference to the 1992 International Swaps and Derivatives Association (ISDA) Master Agreement (Multicurrency Cross-Border form). It is possible to identify two different kinds of issue: the issue brought before the Portuguese courts and related to the choice of jurisdiction, and the issue brought before the foreign courts and related to the choice of law.

The validity of jurisdiction clauses included in swap agreements has been broadly discussed by the Portuguese courts. It is invoked by the aggrieved parties – considering the argument of the banks that the Portuguese courts do not have jurisdiction in the disputes involving swaps agreements under which a foreign jurisdiction was chosen – that the swap agreements are subject to the legal regime of the general contractual clauses, under which the choice of foreign jurisdiction would be invalid as it would cause serious inconvenience to one of the parties.

This argument was upheld once by the Lisbon Court of Appeal in a decision of 10 April 2014,⁴⁴ which considered the jurisdiction clause invalid and deemed that the Portuguese courts had jurisdiction to settle the case. However, this decision was overruled by the Supreme Court,⁴⁵ which has established that the validity of a clause whereby the courts of a Member State are granted the jurisdiction to settle a case should be analysed pursuant to the provisions of Article 23 of the Council Regulation (EC) No. 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, and not pursuant to Portuguese local law. This understanding was confirmed in other decisions.⁴⁶

Further, there is a widely covered dispute that took place in the English courts between a Portuguese bank (which is part of a Spanish financial group) and several Portuguese state-owned companies in connection with several swap agreements (*Banco Santander Totta v. Companhia de Carris de Ferro de Lisboa* [2016] EWCA Civ 1267). Although such swap agreements indicated English law as the applicable law, it was argued by the Portuguese companies that Article 3(3) of the Rome Convention 1980 on contractual obligations applied so as to provide them with defences under certain rules of Portuguese law, considering that the Portuguese legal regime of gaming and wagering, and unexpected changes in the circumstances, should be applied, despite the parties' choice of English law. The Portuguese companies pointed to the fact that the parties were all Portuguese and that all swaps were negotiated and concluded, and ought to be performed in Portugal. However, these arguments were not upheld by the first instance or the appeal courts of England, which considered that the Portuguese legal regime should not be applied since there were a number of elements relevant to the situation that pointed away from Portugal. In particular:

- a the fact that the terms of the swaps allowed for substitution of a non-Portuguese bank in the Portuguese bank's place, coupled with the long-term nature of the swaps – the parties specifically envisaged the possibility of a non-Portuguese bank performing under the swaps at some point;
- b the use of documentation (in the form of the 1992 Multicurrency Cross-border ISDA Master Agreement) specific to the international capital markets, coupled with the fact that the swaps were expressed and confirmed in English;
- c the participation of a Spanish group entity, as a matter of practical necessity, in approving the swaps and providing pricing and other technical support to the Portuguese bank;

44 Proceedings No. 877/127TVLSB.L1-1.

45 Decision of the Supreme Court of Justice of 11 February 2015 (proceedings No. 877/12.7TVLSB.L1-A.S1).

46 Decisions of the Supreme Court of Justice of 8 September 2015 (proceedings No. 542/14.0TVLSB-1), 26 January 2016 (proceedings No. 540/14.4TVLSB.S1), 4 February 2016 (proceedings No. 536/14.6TVLSB.L1.S1), 17 March 2016 (proceedings No. 588/13.6TVPR.T.P1.S1) and 21 April 2016 (proceedings No. 538/14.2TVLSB.L1.S1).

- d* the fact that the swaps were concluded in an international market for over-the-counter derivatives where international banks competed for business; and
- e* the fact that the Portuguese bank entered into back-to-back hedging contracts with a Spanish group entity in circumstances where such arrangements were routine.

VI LOOKING AHEAD

As examined in this chapter, banking litigation in Portugal in recent years has been considerably influenced by the financial crisis. In this context, swap agreements and the mis-selling of investment products by banks shall be highlighted as an important source of litigation involving banks. We believe that this trend will continue in the coming years.

It is important to note that the fall of BES in August 2014 and of Banif in December 2015 has generated numerous disputes, most of which are still pending in the first instance courts. We firmly believe that the core of banking litigation in Portugal in the coming years will be determined by such disputes.

The types of disputes already generated, or yet to be generated, by BES's and Banif's cases are varied:

- a* there is a significant number of mis-selling disputes, since both the banks in question used their network of clients to place investment products issued by their holding companies, which are currently bankrupt;
- b* there are several lawsuits aimed at challenging the resolution measures applied by the BOP to both banks. Naturally, there is great expectation by the market players and most of Portuguese society as to the outcome of these lawsuits; and
- c* the asset-separation criteria used by the BOP are also in the spotlight and there are several lawsuits, with significant amounts at stake, where such criteria are being discussed, particularly in cases where the BOP has decided that debts held by banks to which a resolution measure was applied should stay with the 'bad banks'.

We also envisage that there will be litigation in relation to the liability of directors, senior managers and auditors of the banks that have been subject to a resolution measure.

Finally, another source of potential litigation in the coming years will be the nature and qualification of credits held by banks over insolvent companies, particularly in cases where the bank's role in these companies was not limited to that of a finance partner, but was also to have a substantive controlling influence on the activity of those companies.

SPAIN

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I SIGNIFICANT RECENT CASES

Banking law in Spain has not changed much over the past couple of years; we have had no recent legislative reforms apart from implementing the relevant EU Directives applicable to all Member States. However, there have been some highly significant judicial decisions that have shaped the banking litigation landscape. In particular, there is one decision regarding an institutional investor's multimillion claim against a bank in relation to its initial public offering (IPO)² that has had repercussions and implications for banking litigation in Spain. In view of its significance, we have focused on this decision and analysed the grounds of the judgment in depth because it establishes the path of eventual claims on the IPO of the bank. For this reason, the structure of this chapter differs from others in this publication; where we have not commented on a particular area that other jurisdictions have addressed it is because there is no recent decision of any importance on that topic in Spanish law.

Just a few weeks after the hearing in which the institutional investor in Spain (the 'institutional investor') was suing a Spanish financial institution (the 'bank') for the money it lost when investing in its IPO, the court decided in favour of the bank.

Although the judge, José Ramón Manzanares Codesal, considered that the accounts with which the bank made its debut on the markets were not accurate, he dismissed the claimant's petition for compensation of the €12 million lost of its initial investment of €70 million, and ordered it to pay legal costs.

The judge considered that the institutional investor had not been able to prove that the bank's accounts were crucial to its decision to invest in the bank's shares, and that the error in consent claimed by the institutional investor when entering into the legal transaction, although of an essential nature, was not excusable.

The judge's decision is based fundamentally on the position set out by Spain's Supreme Court at the start of 2016 regarding claims filed by retail investors against the bank.³ In those proceedings, the Supreme Court already held that the bank's accounts did not reflect reality and forced it to refund money to the retail investors.

As the highest court had made a causal link between the bank's false accounting and the essential and excusable nature of the error by investors in general and retail investors in

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2 Ruling No. 70/2017 issued by Court of First Instance 89 of Madrid, Ordinary Proceedings 500/2016, dated 17 March 2017.

3 Ruling No. 24/2016 issued by the Supreme Court in plenary session, Roll of Appeal 140/2015, dated 3 February 2016.

particular, it would appear that the institutional investor's claim should have been received favourably. However, in the process of making the decision, the judge took into consideration a legal concept referred to by the Supreme Court, which is that of 'access to another kind of supplementary information', and the institutional investor appears to have had information that fell within that concept.

Additionally, the judgment states that the claimant received various warnings of 'insecurity and uncertainty' at the bank in the form of downgraded credit ratings by ratings agencies in the days before it was floated on the stock market. Factors that, although made public, are not 'feasible' for retail investors to consult but that the institutional investor was aware of, 'despite which, days later, it decided to acquire almost €70 million in shares'.

In other words, in view of Judge José Ramón Manzanares Codesal, the Supreme Court made it clear that the inaccuracy of the prospectus harmed private small retail investors because they did not have the analytical tools of a large investor, which would be the case for the institutional investor.

The ruling also means a respite for the bank, which was facing the first action brought by a major company, and makes it less likely that it will have to pay out similar compensation to that already paid to retail investors, who had contributed a further €1.8 billion.

In Section II, below, we will analyse the judgment at the Court of First Instance 89 of Madrid in depth in connection with the Supreme Court ruling regarding the same case but applying to retail investors.

II THE JUDGMENT OF THE COURT OF FIRST INSTANCE

i The relief sought by the parties

The institutional investor requested the 'annulment, due to error invalidating its consent, of the two orders of subscription formulated by the Institutional Investor' as well as 'the annulment of the subscription contracts of shares'. Finally, there is a request for payment of the loss suffered on the investment (€12 million), as well as a request for payment of interest and costs.

The bank pleaded for the dismissal of all the petitions raised by the institutional investor.

ii Preliminary issues

The action brought by the claimant

In the case at hand, the following categories of ineffectiveness of legal transactions and agreements recognised in the Spanish legal system are identified:

- a absolute nullity and voidance when a legal provision is contravened (Article 1301 Civil Code (CC)); and
- b annulment or relative nullity if a relevant defect is incurred (usually invalid consent) but there is no contravention of a legal provision or lack of an essential element (Article 1300 CC).

The institutional investor asked for the annulment of a contract with termination effects.

Absence of ad causam standing to sue the alleged by the bank because of the sale of the shares by the institutional investor and the subsequent loss of object

The bank alleged that once the institutional investor sold the shares there was no claim to be brought regarding a legal transaction that no longer existed.

The judge stated that the sale of shares by the institutional investor was sufficient evidence to question the occurrence of the *causa petendi*. According to the Spanish procedural system, claims are based on the occurrence of two elements: *petitum* or relief sought (i.e., what the claimant is asking for); and the *causa petendi*, which are the facts and legal arguments that support the claimant's petitions. Judges are bound by the *petitum* (the judgment must refer to all the petitions made in order to be consistent and should not refer to fewer petitions, more petitions or different petitions than the ones made by the parties) and the facts raised by the parties but not by the legal arguments. This means that the judge may decide about the facts from the standpoint of the different legal arguments or case law applying the principle of *iura novit curia* ('the court knows the law').

The judge argued that, once a legal transaction is extinguished, it seems reasonable that its extinction cannot be declared or constituted again. Therefore, neither absolute nullity nor relative nullity can apply, since there is no contract to undo and the act that the institutional investor says is invalid no longer exists. In short, it is not possible to identify a legal transaction that (still) exists and has effect, and it is also not possible to terminate that legal transaction.

However, because there is no prior ruling in this regard from the Court of Appeal of Madrid or the Supreme Court, the judge dismissed the argument of lack of legal standing to sue raised by the bank.

Expiration of the action

The bank argued that the action brought had already expired.

In this regard the judgment contained a detailed study of the four-year expiration period of the action brought by the institutional investor.

The first day of the limitation period for bringing action for error in consent is when the contract is consummated. To specify the time when the investment contracts are consummated, reference is made to Supreme Court case law, which provides that the consummation of the contract, in order to determine the first day of the limitation period for bringing the action, cannot be fixed before the customer has been able to become aware of the existence of the error or misconduct.

Thus, the first day of the limitation period for bringing the action against the bank was, therefore, the suspension of payment of benefits or accrual of interest, the application of measures of management of hybrid instruments agreed by the Fund for Orderly Bank Restructuring, or, in general, any other similar event that allows for real knowledge of the characteristics and risks of the complex product acquired through erroneous consent.

The events in the case at hand, by virtue of the publicity they were subject to, could not go unnoticed by a qualified or professional investor. It is considered, with certainty, that the institutional investor was aware of the situation that affected the bank's shares on 25 May 2012. Consequently, the lawsuit was filed before the day that the deadline for filing the action expired, which was 9 May 2016.

The expiration defence raised by the institutional investor was dismissed.

iii Grounds and material legal arguments of the case

The core of the judgment contains a study of the error in consent as traditionally applied by Spanish courts and the current approach to erroneous consent in financial contracts given by the Supreme Court in Spain in the past few years as a result of the raising of these sorts of claims because of the global financial crisis.

Classic approach to the error in consent in case law and legal scholars' opinions

The annulment referred to in Article 1300 CC corresponds to the nature of relative nullity, which, referring to the classical doctrine, proceeds by error when the fundamental understanding of the contract is wrong.

In order to make the consent invalid, the error has to fall on the substance of the thing that constitutes the object of the contract, or on the conditions that would have given rise to it (Article 1266 CC). The erroneous circumstance must have been taken into consideration at the time that the contract was finalised.

As the party was bound by the burden of proof, the institutional investor was considered to have been unable to prove in a legally effective manner that the accuracy and certainty of the bank's accounts were essential elements, first to form its knowledge about the circumstances of the legal transaction, and after to form its will to consent to that legal transaction.

In the judge's view, neither the expert witnesses nor any of the other witnesses supported the notion that the bank's accounts were an essential factor for the institutional investor to acquire the shares, as the Court of First Instance deemed that it was clear that the bank's accounts did not fall into the category of main cause to subscribe for the shares but was only an important factor.

The judge understood that the criteria shown to have been crucial for the legal transaction was profitability.

Since the error is not fundamental, the claim should be dismissed, making it unnecessary to analyse the rest of the requirements concerning the error in consent.

But this conclusion is partial, reached only under the classic approach to error in consent in case law and legal scholars' opinions, and it is not the conclusion of the judgment.

III CHANGES TO COURT PROCEDURE

The most interesting part of the judgment is the analysis of the recent case law of the Supreme Court, taking into consideration the absence of High Court rulings on qualified or professional investors. And, specifically, the analysis of the changes that have been applied exceptionally to financial contracts with retail investors.

i Arguments applied in retail investors' contracts

Since 2013 the theory of legal transactions has been modified on an exceptional basis when applied exclusively to financial contracts. In particular, modifications affect four elements of financial contracts:

- a* the assimilation of the error in the consent with the lack of representation or insufficient representation, releasing the investor from liability and transferring that liability to the financial institution;
- b* the non-fulfilment of obligations of financial institutions that has become an essential assumption in the psychological or intellectual consent of investors;
- c* the individualised or tailor-made examination of the essential nature of the error in consent (case by case) has yielded to generalised assumptions; and
- d* if the financial institution has not proved that it has fulfilled its duties, among which is to offer real and accurate information, and the investor breaches those duties, it has to be deemed that the duties were not fulfilled.

The analysis of these modifications and evolution of the assumptions regarding financial contracts makes it possible to understand the considerations that the Supreme Court would reach in the case at hand, where the investor was undoubtedly qualified and professional.

Error in consent: forming the will (lack of representation or insufficient representation)

Although traditionally the Supreme Court had distinguished between error in consent (as a false judgement about the object to which the consent was given) and lack of representation (as a lack of acknowledgment of essential elements in the legal transaction), this difference does not exist when retail investors are involved.

As a rule, the intellectual side of the investor's consent was strictly subjective and the fulfilment of obligations by the financial institution was objective. Now, the fulfilment of the obligations by the financial institution is no longer objective and depends on the characteristics of the retail investor.

In summary, the retail investor is not expected to contract with minimum diligence (the diligence of a 'good family head'); the retail investor is not expected to have studied the contract before signing it even though the clauses of the contract might be clear, simple, concrete and directly comprehensible; and retail investors do not even have to have read the information prospectus received (Supreme Court judgment of 3 February 2016 (Ruling No. 24/2016)).

Duties and obligations of the financial institutions

The Supreme Court has defined the wide scope of the obligations of information that financial institutions are bound by. Such obligations are:

- a* information about the financial product that is the object of the legal transaction and related products so that the retail investor is able to choose mindfully and is aware of his or her choice;
- b* information about the risks of each speculative operation;
- c* information about strategies of investment;
- d* information about orientation concerning the financial products and its strategies; and
- e* warnings affecting those financial products and strategies.

Some rulings also include the presumption of the occurrence of the error in consent if the financial institution has not shown regard for the investor's interests or, further, has not prioritised the investor's interests in case of conflict against its own.

According to the Supreme Court, those duties are a consequence of the asymmetry or imbalance between the information available for a financial institution and the information available for a non-experienced retail investor. The need to protect the retail investor justifies the high standard of information required from the financial institution.

In accordance with securities market regulations (recently reformed in Spain) when financial advice is given, the financial institution should obtain information about the investors in the pre-contractual phase. Only when the financial advice is given to a qualified or professional investor will it be possible to assume that the client has the background and experience needed to understand the investment. The breach of those obligations entails the liability for the damages that investors may suffer.

Essential nature of the error in consent case by case

In the framework of interpretation following the recent judgment, the occurrence of the essential nature of error is presumed when the above-mentioned obligations of the financial institution are breached.

The Supreme Court judgment of 3 February 2016 establishes that the inaccuracies in the information provided by the bank's accounts that are related to the devaluation of its shares removed any expectation of profitability for the retail investors.

Therefore, there is no reason that prevents the application of this consideration to extend to qualified or professional investors.

Obligations breached by the financial institutions

When the investor whose expectations of profitability have not been met argues that the financial institution did not fulfil its obligations, whether the financial institution chooses not to prove that it has complied with those obligations or if it does not because it is impossible (i.e., because of the retirement or death of employees who took part personally in the legal transaction with the client or because the witness from the financial institution is not able to remember clearly and with minimum certainty what happened years ago), courts consider that these obligations have not been fulfilled.

It is clear that financial institutions should be able to prove that the obligation of information was fulfilled. The lack of evidence cannot adversely affect the claimant as that would infringe the principle of ease of access to evidence.

ii The acquisition of shares by the institutional investor

The analysis carried out in the preceding paragraphs is intended to clarify the key facts that resolved the case.

The institutional investor (like most retailers who have filed lawsuits against the bank) grounds its error in consent essentially on the mismatch between the bank's accounting and the reality at the time when the institutional investor made its investment.

Considerations made by the Supreme Court regarding the bank's accounts at the time of the IPO

Since 2012, there has been a criminal procedure in Spain in which the possible criminal consequences of a forgery of the bank's accounts is being examined (misrepresentation of accounts is a crime under Article 290 of the CC).

The existence of a criminal procedure on a particular issue that has an impact on a civil procedure entails the adjournment of that civil procedure until a judgment is handed down in the criminal procedure, as a result of a pending ruling. This would mean the adjournment of the case until there was a ruling on the criminal proceeding regarding the bank's accounting.

However, the pending ruling in a criminal procedure has recently been subject to review by the Supreme Court, no doubt in order to avoid delays caused by adjournments (criminal proceedings usually take longer than civil) and for the reason that the pending ruling could be unnecessary for the assessment of the case. In this regard, the Supreme Court judgment of 3 February 2016 establishes that as the above-mentioned forgery is not material but ideological in nature, the criminal decision about the facts investigated will not have a decisive influence on the resolution of the civil procedure. The assessments respond to different parameters in the criminal and civil procedures. In terms of probative value, a higher standard of proof is required in criminal proceedings than in civil proceedings.

In the case at hand, the expert report provided by the institutional investor was solid in the evidence that the bank's accounts showed inconsistencies with the reality at the time of the IPO. Therefore, for the purposes of judgment of the case, the bank's accounts at the time of the IPO should be considered forged.

The information about the accounts available to the institutional investor: essential nature of the error in consent

Further to the analysis of the case law in the preceding paragraphs applying to retail investors, it is possible to conclude that the protection given by courts to retail investors was justified for two reasons: (1) the lack of financial knowledge; and (2) the forged accounting of the bank.

Focusing on the second issue, the same protection should apply to qualified or professional investors who also made their investment decision based on forged accounting.

In this regard, the main difference between the information considered by the institutional investor and the information considered by retail investors at the time when the decision to invest was made affects complementary reports from financial experts who took into account many economic factors (e.g., interactions, effects, calculations). Those complementary reports made it easier for the institutional investor to have a superior global knowledge of the legal transaction than that available to retail investors, but not in relation to the bank's accounting, to the extent that the institutional investor, having such information that included, for example, the low acceptance of the bank's shares from foreign investors, sold part of its shareholding package to minimise losses and made the investment anyway.

Therefore, taking into consideration that (1) the bank's accounting was declared forged according to civil law (although not, as yet, from a criminal perspective), (2) the bank registered data in the Commercial Registry that did reflect the real data, (3) the bank's accounting was considered an essential element of the investment, and (4) the institutional investor did not have access to accounting information other than that provided by the bank, the institutional investor made an error in its consent that was of an essential and apparently excusable nature.

IV LOOKING AHEAD: FINAL STATEMENT OF THE JUDGMENT AND DISMISSAL OF THE CLAIM

Originally, it would seem that the institutional investor's claim was well grounded and should have been upheld by the first instance court. However, as explained in the introduction, the claim was dismissed. The reasons why are outlined below.

The last part of the judgment starts by referring to another judgment of the Court of Appeal of Madrid (Chamber 14a) dated 21 December 2016, which is one of the few rulings on the bank's IPO regarding qualified or professional investors.

The judgment of the Court of Appeal of Madrid shares the arguments put forward by the Supreme Court in the judgment of 3 February 2016 on the essence of the error in consent, but concludes that the error is inexcusable. According to the Court of Appeal's ruling, the requirement of excusability of the error cannot be assessed for three reasons. In brief:

- a There is a difference between retail investors and qualified or professional investors. Retail investors only have the prospectus as a means of obtaining information on economic data that affect the company whose shares are listed. Qualified or professional investors

may have access to other supplementary information. It is a question of determining whether, based on that supplementary information regarding the bank's IPO in July 2011, the institutional investor's error was excusable.

- b* The bank had lots of investments in the real estate sector and the deterioration of the real estate sector was already known in July 2011 – this could not go unnoticed by the institutional investor, which had to be aware that such exposure to the real estate market could significantly affect the value of the shares.
- c* The regulatory filings made by the bank to the National Securities Market Commission meant that the bank's credit rating was downgraded by the rating agencies before the institutional investor subscribed for the shares.

However, in accordance with the judge, these arguments show inconsistencies. The access to supplementary information was not relevant in the case at hand as it has been shown that such information did not provide any data to prove that the accounts were forged.

Additionally, regarding the bank's investments in the real estate sector, such information was also available for retail investors. It cannot therefore be considered as supplementary information only available to qualified or professional investors. In any case, it has not been possible in the proceeding to prove that such exposure to the real estate sector could potentially affect the value of the shares or that such exposure actually affected the value of the shares.

Given that the Supreme Court causally linked the forged accounting of the bank with the essentiality of the error and with its excusability in general, everything would indicate that the claim should have been successful.

However, the judgment is based on a new concept introduced by the Supreme Court, which lacks a clear legal definition, called 'access to another kind of supplementary information', which it would appear the institutional investor did have: the two rating downgrades made by international ratings agencies that the bank received were prior to the double acquisition of shares made by the institutional investor, and neither of these two downgrades was known to the retail investors of the judgment of 3 February 2016.

Thus, the judge deemed that the institutional investor had two warnings of insecurity and uncertainty regarding the situation of the bank despite which, days later, it decided to acquire shares worth €70 million.

In conclusion, the judge stated that having made such an investment after weighing up the judgements of specialised agencies that recommended caution and in application of the Supreme Court concept of 'access to another kind of supplementary information', the court decided that there were no grounds to uphold the petition for annulment made by the institutional investor in order to recover 18 per cent of its investment. The claim was therefore dismissed.

We expect that the ruling will be appealed before the Court of Appeal of Madrid (and probably, considering the amount in dispute, also before the Supreme Court), so the judgment may change. Nevertheless, the considerations made by the judge and the in-depth analysis of the evolution of the error in consent regarding qualified investors are laudable.

SWITZERLAND

Daniel Tunik, Lorenzo Frei and Téo Genecand¹

I SOURCES OF LITIGATION

The banking industry is an essential economic sector in Switzerland and frequently results in litigation. In most cases, litigation is directed against the banks but occasionally it is initiated by them.

The categories outlined below are among a variety of situations that generate litigation in banking matters.

The issue of bank liability for losses incurred by clients on their deposited assets is one of the most recurring themes in banking litigation in Switzerland. The applicable legal principles, as well as the client's expectations towards banks, vary significantly depending on the legal nature of the relationship between the bank and its client. Typically, this relationship is characterised as 'execution only', 'advisory' or 'asset management' and Swiss courts have developed an abundance of case law setting out the relevant criteria to determine whether the bank is liable for its client's losses.

Overdrafts on client accounts constitute an important source of banking litigation in Switzerland. The most frequent situations are the ordinary foreclosure procedures against pledged real estate as well as procedures on the merits against the client where the overdraft is not covered by any pledged assets. The sudden abandonment of the Swiss franc-euro ceiling by the Swiss national bank in 2015 caused massive losses in the FOREX sector and led to a large number of unsecured overdrafts, in some instances for significant amounts owing to leverage effects.

Enforcing pledges on client assets deposited with banks has generated numerous disputes in instances where banks have attempted to protect themselves against avoidance claims arising from transactions effected for the benefit of their clients, as well as against possible penalties imposed on banks in relation to the undeclared tax status of their clients.

The use of emails and other forms of communication between banks and clients is a regular source of fraud that leads to disputes aimed at determining who should bear the responsibility for the consequences. The actions brought before courts have, in particular, addressed the question of the validity of contractual clauses excluding the bank's liability in situations where it was not able to detect fraud.

In the course of the recent years, data protection issues in the banking industry have kept courts increasingly busy, in particular in the context of the Swiss-US tax dispute and in relation to the transfer of employee data to the United States.

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II SIGNIFICANT RECENT CASES

i Blockage of accounts to secure Madoff clawback exposure

It is common practice that the contractual documentation used by Swiss banks provides for a right of pledge in favour of the bank. Following the bankruptcy of Madoff's fund and the initiatives taken by the trustee in charge of its liquidation, banks took steps to protect themselves against (potential) claims resulting from avoidance actions (clawback). In this context, Swiss banks froze the accounts of their clients who had received redemption payments from funds invested with Madoff.

This approach has been confirmed by Swiss courts in several decisions. In April 2016, the Swiss Supreme Court issued a decision² that recognised the bank's right of pledge as a security for its potential recourse claim related to the risk of clawback.

However, the banks' confidence in the validity of this approach was jeopardised in October 2016 when, in a surprising move, the Supreme Court denied the coverage of such recourse claim for clawback by the general right of pledge of the bank. This case³ related to a client who had opened several accounts with a Swiss bank and signed a general deed of pledge and agreement pursuant to which he granted lien rights to the bank 'as security for all debts and obligations, current or future, in relation with their mutual business relationship'. One of the client's accounts was to be managed by way of a discretionary portfolio management agreement as well as a specific management agreement for investments in risky funds. Between 2004 and 2006, the bank bought, and then sold, several units of two investment funds, which in turn were invested in Madoff. The client had never participated in the decision to make these investments. Further to the clawback actions that had been initiated against the two investment funds, the bank informed its client that a portion of his assets were frozen as security against the bank's potential clawback exposure.

After the first and second instance courts concluded that the bank was entitled to block the account based on the general right of pledge, the client appealed to the Supreme Court. The Court's assessment of this case relied on its case law pursuant to which a general deed of pledge is valid as long as the secured claim is determinable. Potential future claims are deemed determinable provided (1) they are related to the mutual business relationship of the parties and (2) the parties could reasonably expect the occurrence of such claims. The Supreme Court admitted the client's appeal considering that, contrary to the previous judges, even if the recourse claim of the bank did exist (as to which the Court did not decide either way), such claim was not sufficiently foreseeable at the time the client accepted the right of pledge over his assets and thus could not be covered by the bank's right of lien.

The question that arose from this decision is whether the Supreme Court departed from its previous case law with respect to the foreseeability of the bank's recourse claim for clawback risk. The answer is unclear to the extent that the Supreme Court, in its most recent decision, did not discuss or even mention its precedent case issued only a few months before. One of the keys to understanding the different conclusion of this recent ruling may lie in the relationship between the bank and its client. In the case underlying the April decision, the investments had been made further to the instructions given by the account holder, whereas in the other case the client had not instructed the bank to make the relevant investments. The review of the Supreme Court was also limited to the validity of the pledge rights. The

2 4A_540/2015.

3 4A_81/2016.

case was remanded to the lower court for a new decision and the bank may still put forward other theories to justify its right to block the client's assets (e.g., retention right, security for exposure under mandate agreement) meaning that the saga regarding the fate of Madoff clawback claims being heard before Swiss courts may not yet have reached its final stage.

ii Banks' liability for the losses suffered by a client

In the context of execution-only relationships, the bank is under an obligation to execute its client's orders but is not bound by a general duty to safeguard the interests of the client. Accordingly, the principle under Swiss law is that the bank in such relationship shall provide information to its client only upon request. However, over the years, court decisions have held that there are specific situations in which relevant facts should be spontaneously drawn to the attention of the client by the bank. An example of such a case would be if it appears that the client is absolutely unaware of the risks incurred or if a special trust relation has developed over the years between the parties.

In a decision dated 25 April 2016,⁴ the Supreme Court provided further guidance on the bank's special duty of information in the context of execution-only relationships. The judges had to decide whether the custodian bank could be held responsible for the losses caused by the fraud committed by an external asset manager in a situation where the bank had information casting doubts about the reliability of the manager in question. The Supreme Court held that the following circumstances constituted relevant elements triggering a special warning and duty of information even in the absence of any contractual mandate (execution only relationship):

- a* where the bank has doubts about the reliability of the client's external asset manager because of an absolute lack of diversification of the asset management strategy;
- b* where the bank had previously refused to lend money guaranteed by a pledge on part of a fund managed by the client's external asset manager because it considered this to be a guarantee of insufficient quality;
- c* where the bank refused to be the custodian bank for a fund managed by the client's external asset manager because it could not understand its functioning; and
- d* to a lesser extent, where the bank had knowledge of negative press coverage on the directors of the client's external asset manager, even though the press coverage did not concern a matter that was financial in nature.

By contrast, in another decision dated 14 September 2016,⁵ the Supreme Court found that the bank had complied with its duty of care by informing its client that it had suspicions of potential criminal conduct by the external asset manager. The judges held that the bank was not expected to take additional precautionary measures on behalf of the client, it being specified that in this case the client did not react despite the alarming information provided by the bank.

In 'asset management' relationships, the bank undertakes to manage all or part of the client's assets at its discretion but in accordance with the strategy, limits and objectives set with the client. In contrast with execution-only relationships, under asset management relationships, the bank has an extensive duty of information, as well as a duty to take whatever measures are necessary to safeguard its client's interests.

4 4A_369/2015.

5 4A_361/2015.

In addition to the execution-only and asset management relationships, banking practice has developed an intermediary relationship, namely the 'advisory' relationship. This covers a wide variety of situations ranging from a mandate that, in many ways, is similar to an asset management mandate through which the investment decisions are taken directly by the client but on the basis of the bank's regular advice, to relationships with one-off advice given by the bank. The bank's duties to inform and advise the client depend on the type of advisory contract as well as on other prevailing circumstances, such as the client's knowledge and experience in banking and finance matters. As a matter of principle, Swiss law considers that the client bears the risks of the transaction if it follows the bank's advice, unless the advice was patently unreasonable at the time it was given.

On 18 April 2017, the Supreme Court reviewed a case⁶ in which clients had invested in a Lehman Brothers structured product recommended by the bank. The investment was made in January 2007 and resulted in a near-total loss following the bankruptcy of Lehman Brothers. The clients claimed that the bank's presentation of the product as being a guaranteed-capital structured product was misleading and that they were not (sufficiently) made aware of the risk of issuer. The Supreme Court ruled that this was not relevant. At the time of the advice, the issuer risk related to Lehman Brothers was minimal according to financial experts. Additional explanations on the risk of issuer would thus not have discouraged the clients from investing in the contentious product. Further, as the bank had not given any recommendation as regards the amount to invest, the bank was not expected to warn the clients about the risks associated with an absence of diversification, even though the clients had invested approximately half of their savings in the contentious product.

The question that courts face regularly relates to the calculation of the damages that the client may claim in the event of a breach by the bank of its duties.

In a recent case, the Supreme Court recalled the quite strict requirements regarding the demonstration of the damages.⁷ The case involved a relationship manager who had performed unauthorised transactions on a client's account. Following the discovery of the fraud, the client sued the bank for US\$6 million claiming that this amount corresponded to the difference between the value indicated on the false statements provided by the relationship manager and the effective value of his portfolio. In the course of the proceedings, the client had offered another method to demonstrate his damages based on the difference between his initial investment and the profit of approximately 2.8 per cent gained by a similar portfolio during the same period. The lower court considered that the exact amount of damages could not be determined and, by making an estimate, awarded the client US\$5.7 million. Following an appeal of the bank, the Supreme Court overruled the decision of the lower court and dismissed the client's claim. The Supreme Court held that, since it was possible to individualise the wrongful investments, the client was in a position to determine precisely his damages. This is done by calculating the difference between the actual value of the investments and the hypothetical value that they would have if they had been performed according to the agreed strategy. Hence, the client should have demonstrated his damages for each wrongful transaction, which he did not do. This leads to the dismissal of the client's action.

6 4A_403/2016.

7 4A_586/2017.

III CHANGES TO COURT PROCEDURE

Switzerland is a federation. Pursuant to the Constitution, material civil law and debt enforcement procedures are governed by the federal state and have been unified thereunder for over a century. By contrast, the authority to legislate on the rules regarding civil procedure remained with the cantons, as a result of which civil proceedings in Switzerland were characterised by the existence of 26 different procedural civil laws. This was eventually deemed to be excessively burdensome, costly and an obstacle to the predictability of proceedings. After a lengthy process, a federal Code of Civil Procedure (CPC) entered into force as of 1 January 2011 and replaced the previously existing cantonal laws.

Although the unification of the rules of civil procedure did not fundamentally modify banking litigation, it has certainly made it easier for lawyers to appear before other cantonal courts. In that respect, the change in question may be considered to make access to courts easier for clients. There is an ongoing review of the CPC. The major change of the current draft is the additional possibilities for collective action (currently not admissible to claim damages). Additional suggested amendments include considering that attorney privilege also covers the work of in-house attorneys in civil proceedings, a new procedural status for reports of private experts and reduction of the amount of the advance on judicial fees.

IV ATTORNEY–CLIENT PRIVILEGE

Attorney–client privilege, in particular its scope, can raise questions in the context of banking litigation. This happens, in particular, when litigation is related to situations where the factual background is complex and requires fact-finding activities. In such situations banks often decide to carry out internal investigations, which can be conducted by lawyers.

This activity is generally considered to be covered by the attorney–client privilege. This is based on the general rule that provides that attorney–client privilege covers typical activities of a lawyer, such as legal representation, provision of legal advice and drafting of legal documents. Other activities, such as serving as a director, asset manager, testamentary executor or trustee, are regarded as atypical activities for which this particular protection is not justified and are thus not covered by attorney–client privilege. This distinction is, however, not always clear and some activities are considered mixed.

A decision by the Supreme Court made on 20 September 2016⁸ caused particular concern in the legal community and illustrates the types of difficulties that may arise where the tasks carried out by lawyers may be viewed as overlapping with activities that a bank would be compelled, by law, to conduct. The case involved a Swiss bank, whose employee – a wealth manager – was the subject of a criminal investigation in relation to a corruption matter involving Greek officials. In this context, the bank mandated two law firms to carry out an internal investigation to determine if anti-money laundering legislation had been violated. The internal investigation also included the review of the bank's internal notes and the interviewing of its employees. The question arose as to whether the work product of the bank's attorney was covered by attorney–client privilege after various documents, including memos and minutes of interviews, were seized in the context of the criminal investigation. Following an appeal by the bank, the Supreme Court considered that the results of the internal investigation were not entirely covered by attorney–client privilege. In order to

8 1B_85/2016.

understand the reasoning of the Supreme Court, it must be noted that the Anti-Money Laundering Act (AMLA) imposes on Swiss banks (and other entities concerned) a duty to document transactions and clarifications carried in a manner enabling a third party to make a reliable assessment of the transactions and business relationships, and of compliance with the provisions of the AMLA. In the case at hand, the judges held that the fact-finding work done by the bank's attorneys was part of the bank's duty to document the clarification work done and that the bank had in fact delegated its duty to its attorneys. The Supreme Court concluded that this work could not be subject to attorney-client privilege, otherwise it would mean that the AMLA provisions could be circumvented by delegating these duties to attorneys. The Supreme Court confirmed this ruling on 21 March 2018,⁹ in a procedure directed against representatives of a bank for violation of their duty to report a case under the AMLA.

The lesson out of these rulings is that attorneys and banks should be aware of this issue and take the appropriate steps before and during the performance of an internal investigation to isolate the information covered by attorney-client privilege from the rest of their (fact-finding) work.

V JURISDICTION AND CONFLICTS OF LAW

Swiss banks usually provide in their general terms and conditions that the contract shall be governed by Swiss law and that Swiss courts shall have sole jurisdiction over any dispute. In the context of clients residing abroad, the question that arises is whether Article 15, Paragraph a(c) of the Lugano Convention (CL) may result in setting aside such contractual agreement.

In its ruling dated 9 February 2016,¹⁰ the Supreme Court considered that the client of a Swiss bank falls under the broad definition of a consumer within the meaning of Article 15 of the CL. However, in order to set aside a jurisdiction and choice of law clause, the bank's client had to prove that he was actively solicited by the bank in his country of residence at the outset of the relationship.

In the context of foreign proceedings, banks also frequently face document production orders issued by Swiss authorities following an international mutual assistance request be it in administrative, criminal or civil matters. In civil proceedings, when banks are ordered as third parties to produce documents, they may – or shall, based on their contractual relationship with the client – try to dismiss the order based on the argument that banking secrecy should prevail on the interest to produce the documents in the civil procedure pursuant to Article 166, Paragraph 2 of the CPC. The Swiss judge shall weigh up both interests and decide whether to maintain the order. In Swiss proceedings, the client to whom the documents are related is not in a position to intervene in this process. The Supreme Court rendered an interesting decision setting different standards in the context of international mutual assistance in civil matters in a dispute where the Hague Convention of 18 March 1970 (HC70) on the taking of evidence abroad in civil or commercial matters was applicable. In its decision dated 21 December 2015,¹¹ it indeed considered that the client – if he or she is not a party to the foreign procedure – shall be heard in this procedure before any production order may be addressed to a Swiss bank through the channel of international civil mutual assistance. If the client had not been heard in the foreign procedure, the international civil mutual

9 1B_433/2017.

10 Published under ATF 142 III 170.

11 Published under ATF 142 III 116.

assistance request was to be rejected based on Article 12, Paragraph 1(b) of the HC70. In a decision dated 29 August 2017,¹² the Supreme Court specified that the client has to inform the foreign judge that he or she disputes the request for international mutual assistance and requests to be heard if he or she wishes to assert rights under the above-mentioned case law.

VI EXCLUSION OF LIABILITY

As a matter of legal principle, banks bear the risk of executing orders from unauthorised persons. Indeed, to the extent that a bank executes a payment without having validly received an order to this effect from the client, the bank is not authorised to debit the client's account in order to cover the amount of the transfer. However, banks usually include a clause in their contractual documents and general conditions that shifts this risk onto the client. Pursuant to Article 100 of the Swiss Code of Obligations (CO) – applicable by analogy to this type of clause – such transfer of risk is not valid in the case of serious misconduct or gross negligence on the bank's part. In the event the behaviour is attributable to officers with functions falling within the meaning of corporate bodies, the transfer of risk may be considered as invalid, even in the case of mere negligence.

As regards the bank's duties when it receives a transfer order, it is generally admitted that banks are required to verify the authenticity of orders only within the limits agreed by the parties, unless the circumstances surrounding the order give rise to doubts and warrant to carry out additional checks.

In a decision dated 5 December 2016,¹³ the Supreme Court ruled that the following elements are to be considered when assessing whether the circumstances warrant carrying out additional checks before executing an order:

- a* where the style of the communications issued by the client change dramatically, such as by suddenly using poor vocabulary and containing syntax and spelling errors despite being written in the native language of the client;
- b* where the timing or beneficiary of the order given is unusual for the client. In the case at hand, the first order emanated from a hacker and was only the second exit of funds ordered in the past 10 years and the first in favour of a third party who was neither located in Switzerland nor in the home country of the account holder. The bank unsuccessfully argued that in view of the rarity of transfers it was not possible to determine what was usual for this account, as the client had on several occasions indicated that he held this account to diversify his funds in Swiss francs as well as for the purposes of safety and stability;
- c* where the amount of the envisaged transfer is unusual for the client. In the case at hand, the first order involved nearly a quarter of the assets under management despite the fact that the client had wired the majority of his assets to his Swiss account a few months before and mentioned that they represented his savings and were intended to be kept long-term;
- d* where the cause of the transfer is not specified immediately despite the fact that the client usually shared spontaneously his intended actions and the underlying reasons for them;

12 4A_167/2017.

13 4A_386/2016.

- e* where the order is required in an urgent manner without clear reasons justifying the need to act quickly; and
- f* where an executed order is only signed with the first name of the client and not with the signature known by the bank.

The general conditions of banks usually contain a clause pursuant to which the client is deemed to have accepted an order in the absence of reaction within 30 days. The Supreme Court did, however, confirm that this legal fiction of ratification of the order is to be disregarded in situations where the client actually never received the information in relation to the transfers, such as for hold mail accounts.

In the context of this decision, the Supreme Court addressed the disputed question of the impact of the client's contributory negligence. In other words, can a bank argue that a client's claim is to be reduced or discarded by virtue of the fact that the client contributed to the damage by reason of its negligence or reckless conduct? The Supreme Court took a formal and strict approach by stating that the client, in this type of situation, is not entitled to seek damages strictly speaking, but rather the mere performance of the contract by prohibiting the bank from debiting the client's account on the basis of an authorised order. In such cases, according to the Supreme Court, the indemnity cannot be lowered as a result of contributory negligence within the meaning of Article 44 of the CO. On the other hand, the judges considered that the bank could assert its own claim against the client by invoking a breach by the client of its contractual obligations resulting in damages caused to the bank (i.e., the fact that it had to pay the third party without being in a position to debit the client's account to cover the payment in question). In practice, this means that the bank may not simply oppose the client's contributory negligence in its defence against the client's claim, but has to prove that the conditions for a contractual or tort liability against the client are met, which is undoubtedly more difficult to prove.

In a decision dated 15 June 2017,¹⁴ the Supreme Court ruled that if an order is unusual, the bank should, in principle, contact the client directly and not a third party with a power of attorney on the account. In the case at hand, an asset manager had meticulously forged the signature of her client to order transfers. The bank had identified that the transfers were unusual, but called the external asset manager – who had the necessary power of attorney to order the relevant transactions – to ensure that the orders reflected the client's intent. This was considered a serious misconduct on the bank's part.

VII REGULATORY IMPACT

As a matter of principle, Swiss regulatory rules usually aim at protecting public interests – rather than private interests – and thus do not apply directly in the private law relationships between banks and their clients. For example, the Supreme Court stated in a decision¹⁵ that a person could not base a liability claim against a bank solely on a violation of regulatory rules (such as the one provided in the AMLA); the person has to prove that a law protecting his or her own private interests was violated by the bank, such as money laundering pursuant to Article 305 *bis* of the Swiss Criminal Code in order to have valid grounds for a liability claim.

¹⁴ 4A_379/2016.

¹⁵ Published under ATF 134 III 529.

That said, there has been an increasing number of exceptions to this principle with regulatory provisions that envisage specific liability claims. By way of example, Article 145 of the Federal Act on Collective Investment Schemes provides that all persons involved with the establishment, management and distribution of the fund (e.g., the custodian bank) are subject to direct liability towards individual investors and other creditors of the company.

The Swiss Federal Council's message accompanying the draft Swiss Federal Financial Services Act (FFSA) and the draft Swiss Federal Act on Financial Institutions (see Section VIII, below) state that the various prudential rules that the actors of the financial sector will be expected to comply with are regulatory rules that are not directly applicable to client-bank relationships. They do, however, point out that civil judges will be able to review these obligations to interpret and clarify the applicable civil obligations. This approach highlights the increasing impact of regulatory rules and its impact on civil banking litigation.

VIII LOOKING AHEAD

Following the 2008 financial crisis, as well as the international developments in financial regulations in general, the Swiss Federal Council has been actively involved in the enactment of two new pieces of legislation that will have an impact on the financial sector as a whole: the FFSA and the Swiss Federal Act on Financial Institutions. These two laws are still in draft form and will be subject to further discussion and amendments at the federal parliament. Without entering into detail, it can be said that several provisions of the FFSA are likely to impact the procedural rules governing disputes arising between banks and their clients. As an example, the current version of FFSA provides for the possibility to opt for a mediation procedure as an alternative to the mandatory conciliation procedure. In addition, there are discussions regarding the enactment of a rule that would exclude the possibility for banks to claim an indemnity for legal fees – as is usually the case in Switzerland for the successful party to a litigation – except where the amount in dispute exceeds a certain level. Although it is still uncertain whether these changes will eventually be enacted, they certainly reflect the prevailing trend that aims to favour the position of clients in relation to banks in the context of litigation. Banking litigation will undoubtedly continue to evolve in Switzerland.

TAIWAN

Patrick Marros Chu, Salina Chen, Joyce W Chen and Chi Lee¹

I OVERVIEW

In Taiwan, the financial crisis of 2008 has led to several recent legislative developments. The array of disputes regarding target redemption forward foreign-exchange-related derivative financial products (TRFs) in 2014 and 2015 further resulted in a vigorous debate among regulators, financial institutions and consumers regarding consumer protection in financial services.

II SIGNIFICANT RECENT CASES

i Taiwan High Court civil judgment 106-Zon-Shan-Zi-646 (2017)

The plaintiff, a commercial bank, claimed against the defendant, a foreign corporate investor, for the proceeds from certain TRF transactions entered into between the parties. The district court ruled against the plaintiff on the ground that the plaintiff failed to fulfil its obligation to disclose the investment risks to the investor before the transaction, thereby causing the defendant to be unable to properly assess the potential transaction risks beforehand. The district court's decision was among the very few cases in which the court ruled against the financial institutions in similar disputes. However, on appeal, the Taiwan High Court overruled the district court's decision and concluded that the plaintiff was not required to provide such risk alert to a professional investor such as the defendant, and therefore the plaintiff's claim was with merit.

ii Taichung District Court civil judgment 103-Su-Zi-3271 (2016)

The plaintiff, a corporate investor, alleged that the defendant, a commercial bank, violated relevant selling restrictions when selling certain TRFs to the plaintiff, and argued that the transaction should be void. The plaintiff further asserted that the defendant failed to perform a suitability test on the plaintiff regarding the TRFs and committed fraud; therefore, the plaintiff should have the right to cancel the transaction. The Taichung District Court ruled in favour of the defendant. The court held that the TRFs are not covered by the selling restriction and a bank can legally sell such product in Taiwan through its offshore banking unit (OBU). The court further ruled that the defendant had provided sufficient disclosure documentation to the plaintiff, including presentation decks, the product terms and conditions, and certain risk-alert documents to the plaintiff, and the plaintiff was fully aware

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of the risk to the transaction. The court also held that the defendant had duly performed suitability analysis on the plaintiff's risk endurance level. In sum, the transaction between the plaintiff and the defendant was legally effective, and the defendant was not liable for the investment loss suffered by the plaintiff.

iii Supreme Court civil judgment 102-Tai-Shan-Zi-1189 (2013)

The Taiwan High Court held that a bank failed to fulfil its duty of disclosure to an investor because the disclosure documents were complex and difficult to read. The Taiwan High Court also held that the investor's signature on the disclosure document alone cannot prove that the bank had properly disclosed the investment risk to the investor. The Supreme Court of Taiwan vacated the Taiwan High Court's decision and remanded the case for further investigation of evidence on whether the bank fulfilled its duty of disclosure. The remanded case was subsequently resolved through mediation.

Since the establishment of the Financial Ombudsman Institution after the promulgation of the Financial Consumer Protection Act in 2011 (the FCP Act), most of the banking disputes involving financial consumers in Taiwan that were traditionally decided by courts through litigation are now resolved by the Financial Ombudsman Institution.² The Taichung District Court judgment described in subsection ii, above, is one of the few disputes resolved through civil litigation in recent years. Many other cases were resolved through settlement or mediation, such as the Supreme Court judgment outlined above. The FCP Act does not apply to banking disputes involving offshore branches, OBUs, qualified institutional investors, or persons or entities with a certain level of assets or professional investment intelligence prescribed by the competent authority from time to time.

III RECENT LEGISLATIVE DEVELOPMENTS

i General regulatory scheme of financial institutions

The regulations of financial institutions in Taiwan are generally imposed by the Financial Supervisory Committee. The sale of financial products is generally regulated under the Banking Act with regard to the sales by banks, and the Securities Exchange Act with regard to the sales by securities firms. There are also other relevant regulations authorised by the two aforementioned acts, such as the Regulations Governing Foreign Exchange Business of Banking Enterprises, the Regulations Governing Foreign Exchange Business of Securities Enterprises, the Regulations Governing Internal Operating Systems and Procedures for Banks Conducting Financial Derivatives Business, and the various orders and opinion letters issued by the competent authorities from time to time.

In general, a financial institution is required to submit a proposed financial product, such as a fund or a bond, to the regulatory authorities for their review. The purpose of such submission is to ensure that the financial product is properly designed and the relevant information is properly disclosed in the transaction documents. Approvals by the regulatory authorities must be obtained before the financial institution can sell the product to a customer. Nevertheless, a structured product is usually sold through the structure of 'specific monetary trust' in Taiwan and the trust agreement governing the transaction of the structured product is generally deemed a private contractual relationship between the financial institution and

² See Section III.iii, below.

the investor. An investor entrusts his or her money to a domestic financial institution, which in turn invests the entrusted money in an offshore structured product based on the trust agreement. As such, unlike funds or bonds, the regulatory authorities are not required to review these products prior to the transaction. Prior to the 2008 financial crisis, a wide variety of structured products were therefore sold to many investors without adequate regulatory review or approval.³

Given the commonly used investment structure mentioned above, the financial institutions are also governed by the Trust Law as trustees of the trust properties. Pursuant to the Trust Law, a trustee should manage the trust matter with the due care of a 'prudent administrator'.⁴ When a trustee fails to manage the trust matter with such due care thereby causing the settlor any damages, the trustee is liable to the trust property for such damage.⁵

ii Additional regulatory requirements in response to the financial crisis

In light of the 2008 financial crisis and in response to the call from the public for more stringent regulations, the Regulations Governing Offshore Structured Products were promulgated, which target a specific category of financial products, namely, the offshore structured products. The Regulations set forth the requirements for the sale of offshore structured products, including, among others, the requirements for Chinese disclosure documents,⁶ the obligation of the financial institutions to explain to the investors whether the product is principal guaranteed⁷ and the obligation of the financial institutions to read out the disclosure documents to the investors and to record such conversation.⁸ Although the regulations provide rather detailed guidelines regarding the sales by financial institutions, they do not cover the general regulations of other financial products.

During 2014 and 2015, many small to medium-sized corporations in Taiwan invested in TRFs (as defined in Section I, above) and suffered serious losses. In response to these cases, the Financial Supervisory Committee further set forth a series of regulations on 'complex, high-risk derivative financial products' (e.g., the Regulations Governing Internal Operating Systems and Procedures for Banks Conducting Financial Derivatives Business). These regulations provide a detailed definition on what kind of products constitute 'complex, high-risk derivative financial products'. In general, the products with higher risk and higher leverage will more likely fall into this category, which also includes offshore structured products.⁹

iii Financial Consumer Protection Act Enacted in 2011

In response to the need for a more stringent regulatory scheme on a wide array of financial products, the FCP Act was promulgated in 2011. The FCP Act has two major regulatory purposes. It aims to provide general regulations covering more categories of financial

3 Li-Chung Lee, 'Analysis on financial product sale disputes and cases', *Taiwan Bar Journal*, 2009.8, at 25–27.

4 Trust Law, Section 22.

5 Id., Section 22.

6 Regulations Governing Offshore Structured Products, Section 9.

7 Id., Section 23.

8 Id., Section 22.

9 Regulations Governing Internal Operating Systems and Procedures for Banks Conducting Financial Derivatives Business, Section 2.

products, and replaces the prior rules that were scattered in several different laws and regulations. Additionally, the FCP Act also sets forth a new mechanism for the financial disputes resolution procedures.

The FCP Act applies to disputes between a financial institution and a financial consumer with regard to provision of financial products and services.¹⁰ The financial institutions regulated under the FCP Act do not include offshore branches and OBUs.¹¹ The FCP Act also specifically narrows its application to ‘financial consumer’ and excludes its application to investors such as qualified institutional investors and persons or entities with a certain level of assets or professional investment intelligence prescribed by the competent authority from time to time.¹²

The major aspects of the FCP Act include, among others, the due care obligation of a financial institution when selling financial products or providing services; the truthfulness obligation of a financial institution when soliciting customers, promoting products and advertising; the obligation of disclosure; the obligation of evaluation of suitability of certain products to a consumer; and the responsibility of the financial institution for failure to fulfil these obligations. The FCP Act specifically provides that a financial institution should bear the duty of due care of a ‘prudent administrator’ to an investor when providing financial products or services.¹³

Furthermore, the Financial Ombudsman Institution was established under the FCP Act in 2012. The Financial Ombudsman Institution is the major focus of the new alternative dispute resolution mechanism. Under the new mechanism, when a financial consumer dispute arises, the financial consumer reports first to the financial institution with which the consumer has a dispute. If the solution proposed by the financial institution is not satisfactory to the consumer or if the financial institution fails to review the case, the consumer can then apply to the Financial Ombudsman Institution for an ‘ombudsman case’.¹⁴ The ombudsman case will be reviewed by an ombudsman committee.¹⁵ If the applicant accepts the decision of the ombudsman committee, the financial institution should also accept the decision if (1) it is under the amount prescribed by the competent authority, or (2) the applicant is willing to reduce the amount of the case to a figure below the prescribed amount.¹⁶ The applicant can then apply to the court for the court to approve the decision of the ombudsman committee.¹⁷ A decision approved by the court has the same legal effect as a court judgment.

Since its establishment, the Financial Ombudsman Institution has reviewed hundreds of cases. During 2015, 2016 and 2017, the Institution reviewed 235, 278 and 244 cases, respectively, with regard to banks, and 37, 38 and 44 cases, respectively, with regard to securities firms.¹⁸

10 FCP Act, Section 5.

11 Financial Supervisory Committee Letter Jin-Guan-Fa-Zi No. 1010070279.

12 FCP Act, Section 4.

13 FCP Act, Section 7.

14 FCP Act, Section 13.

15 FCP Act, Section 17.

16 FCP Act, Section 29.

17 FCP Act, Section 30.

18 www.foi.org.tw/Article.aspx?Lang=1&Arti=2560&Role=1. (Last visited on 19 May 2018.)

IV FREQUENT CAUSES OF ACTION

The major source of banking litigation in Taiwan is between financial institutions and individual investors in the financial product retailing market. In the litigations regarding investment product retailing, the most common causes of action include:

- a* failure in the formation of contract;
- b* failure of a financial institution in fulfilling its duty of disclosure;
- c* failure of a financial institution in evaluating consumer suitability in investing in a specific product;
- d* failure of a financial institution in fulfilling the post-transaction duty of disclosure; and
- e* violation of sales limitations.¹⁹

Each of the categories is further elaborated on in this section, while (b) and (d) will be addressed together as the general duty of disclosure of financial institutions.

i Formation of contract

Entering into a contract through an agent

One of the common disputes that arises between a financial institution and an investor is whether the agent of the investor has the authority to enter into a contract on behalf of the investor. Based on banking practice in Taiwan, it is very common for an investor, as a principal, to delegate to an agent by giving the agent the investor's name chop (which has the same legal effect as a signature in Taiwan) and, sometimes, the identification document.

In a case before the Taiwan High Court in 2011, the investor delegated his spouse as an agent, by giving his spouse his name chop, to renew his deposit contract with a bank. The spouse instead purchased a structured product on behalf of the investor. The investor subsequently accepted the interest distribution of the structured product without any objection.²⁰ The issue then was whether the agent had the authority to purchase a structured product for the investor, and whether the investor recognised such authority by accepting the interest distribution. The court ruled that (1) although it is common for spouses to have each other's name chop for daily transactions in Taiwan, the renewal of a deposit and the purchase of a structured product have different investment risks in nature, and (2) the bank failed to verify with the principal regarding the agent's scope of authority, which the bank could have known had it simply contacted the investor for verification; therefore, the fact that the agent possessed a name chop was insufficient to prove that the agent had the requisite authority.²¹ The fact that the spouse entered into a structured product contract without authority, therefore, rendered such contract invalid. Furthermore, even though the investor subsequently accepted the distribution payment without any objection, the investor did not explicitly recognise or promise to be bound by the spouse's action.²² However, it is worth noting that the majority of the Taiwanese courts used to hold the opinion that the presentation of a name chop can establish that the agent has effective presence of authority

19 See Chen, Christopher Chao-hung, 'Legal Risk and Investor Protection for Retail Investment Products: An Empirical Study of Lawsuits Regarding Mutual Funds and Structured Notes in Taiwan', *Chengchi Law Review*, 2014.2, at 153.

20 See Taiwan High Court civil judgment 100-Shan-Zi-202 (2011).

21 *Id.*

22 *Id.*

as long as the agent also presents other forms of documentation in addition to a name chop, such as a cheque book or a receipt.²³ Given the above, it remains uncertain as to whether a financial institution is under the burden of further verifying the authority of an agent or can simply rely on the presentation of the name chop of the investor.

Delivery of investment documents

The investors asserted in some cases that the financial institutions failed to deliver proper documentation when entering into the investment contracts with the investors. A court held that failure of the financial institution to deliver proper documentation should be deemed non-performance of the contract.²⁴ However, it is of the view that so long as the financial institutions have duly delivered the Chinese offering circulars or disclosure documents, the fact that the original English offering circulars or disclosure documents were not delivered to the investors would not affect the formation of a contract.²⁵

Cancellation of contract

In some situations, a court will allow the investor to exercise its right to cancel the investment contract, such as in cases of fraud. In a case before the Taipei District Court, a financial institution failed to properly specify in the contract or to explain to an investor the exact items, amounts and calculations of the fees and commissions. By withholding important information such as the existence of relevant service fees payable by the investor, the financial institution was deemed to have withheld information and committed a fraud, and the investor would be entitled to the right to cancel the investment contract.²⁶

ii Duty of disclosure of financial institutions

Disclosure upon sales

A financial institution is generally obligated to disclose certain essential information during the process of transaction as a seller of a financial product. The duty and scope of disclosure of a financial institution upon selling financial products are generally regulated by the Financial Supervisory Commission in its various administrative orders. Nevertheless, before the promulgation of the Regulations Governing Offshore Structured Products in 2009, the specific disclosure obligation of financial institutions on the sale of structured products was less regulated than other financial products.

One of the major issues here is whether the signature of the investor on the disclosure documents is sufficient to prove that the financial institution has properly delivered such disclosure documents to the investor or fulfilled its disclosure obligation. Most courts are of the view that if the investor signed a document with sufficient disclosure of investment information, the signature itself is sufficient to prove that the financial institution has fulfilled its disclosure obligation prior to and upon the transaction, such as in Taiwan High Court

23 See Supreme Court civil judgment 44-Tai-Shan-Zi-1428 (1955). See also Supreme Court civil judgment 56-Tai-Shan-Zi-2156 (1967). See Wu, Jiin-Yu, 'The exclusion of the principles responsibility for apparent agency', *Taiwan Law Journal*, 2013.12, at 189.

24 See Taipei District Court civil judgment 98-Zon-Su-Zi-195 (2009).

25 See Taiwan High Court civil judgment 98-Shan-Yi-Zi-672 (2009).

26 See Taipei District Court civil judgment 97-Su-Zi-5116 (2009).

civil judgment 98-Zon-Shan-Zi-288.²⁷ On the other hand, in another case, the court ruled that if the investor in fact signed the disclosure document under the instruction of the sales representative, the signature cannot serve as the evidence that the sales representative has fulfilled the financial institution's disclosure obligation.²⁸ In a more extreme case, the Taiwan High Court held that the signature alone is insufficient to prove that the financial institution has fulfilled the obligation of disclosure.²⁹ However, very few courts have adopted such view.

Another common argument made by the investors is that the transaction documents are too complicated in form and in written language, and are difficult or impossible for the investors to understand. In a case before the Taiwan High Court Taichung Branch, the Court ruled that so long as the documents clearly specified the investment risks, and alerted the investors to such risks, the fact that some parts of the documents are complicated did not prevent the investor from understanding the investment risks.³⁰ Another case before the Taiwan High Court, however, ruled that if the layouts of the transaction documents were too difficult to read and comprehend, the delivery of such document was not sufficient to prove that the financial institution had fulfilled its disclosure obligation.³¹

Another issue that frequently surfaced during litigation is the scope of the duty of disclosure, namely, how much information a financial institution is obligated to disclose. In the same case before the Taiwan High Court, the financial institution that failed to disclose to the investor about the nature of the product as a structured product without principal guarantee, as well as other risks, was held by the court to have violated the financial institution's duty of disclosure to the investor.³² In another case, the court held that the financial institution had made sufficient disclosure by providing the disclosure document that specifies the structure of the product, the annual return rate calculation and the risk alert regarding potential loss at the event of early redemption.³³

In addition to the general disclosure obligation as the seller, in an investment structure of specific monetary trust as mentioned in Section III.i, above, the financial institution, as a trustee, is also obligated to act in accordance with the due care of a 'prudent administrator'.³⁴ The courts generally held that a financial institution should bear such obligation at the time of entering into a specific monetary trust agreement. A financial institution that fails to provide sufficient disclosure when selling structured products violates the due care of a prudent administrator and should be liable for the damages suffered by the investor, as the settlor.³⁵

Continuing duty of disclosure

The financial institutions' continuing duty of disclosure, or post-transaction duty of disclosure, is usually raised in trust cases. The background of such issue is that when the 2008 financial crisis gradually unfolded, many financial institutions failed to alert the existing investors

27 See Taiwan High Court civil judgment 98-Zon-Shan-Zi-288 (2010).

28 See Taiwan High Court Tainan Branch civil judgment 99-Shan-Yi-Zi-157 (2011).

29 See Taiwan High Court civil judgment 99-Zon-Shan-Zi-45 (2010).

30 See Taiwan High Court Taichung Branch civil judgment 99-Shan-Zi-26 (2010).

31 See Taiwan High Court civil judgment 99-Zon-Shan-Zi-45 (2010).

32 See Taiwan High Court civil judgment 99-Zon-Shan-Zi-45 (2010).

33 See Taiwan High Court Tainan Branch civil judgment 99-Jin-Shan-Yi-Zi-1 (2011).

34 Trust Law, Section 22.

35 See Taiwan High Court civil judgment 98-Shan-Yi-Zi-299 (2010).

regarding the change of risks in their investments. A financial institution, as a trustee in a specific monetary trust, is generally obligated to report necessary information of the trust property to an investor, as the settlor, such as the change in value of the trust property.³⁶

Nevertheless, the courts remain split as to whether the financial institution has the general obligation of continuing disclosure of potential risks after it enters into a transaction. In the Taiwan High Court civil judgment 99-Zon-Shan-Zi-45, the court decided that the financial institution should inform the investor of the subsequent material change of the product risk.³⁷ However, another court is of the view that there are too many factors affecting the change of product risk and, therefore, the burden of notification should not be placed on the financial institution that sold the products.³⁸

It is worth noting that the plaintiffs in a substantial portion of cases in structured bond disputes raised the argument based on financial institutions' continuing duty of disclosure.³⁹ Nevertheless, the FCP Act does not elaborate on or provide clarification regarding financial institutions' continuing duty of disclosure to the consumers.⁴⁰ It is anticipated that the disputes in the future, to be resolved either through litigation or through the Financial Ombudsman Institution, will still focus on the continuing duty of disclosure, considering the lack of clear regulations and judicial guidance.

iii Consumer suitability

Prior to 2009, there were no laws or regulations that clearly set forth a financial institution's duty to evaluate or monitor a consumer's suitability in investment in terms of risk-bearing ability other than the financial institution's internal policies. It is usually argued by the financial institutions that they have fulfilled their duty to evaluate a consumer's suitability in investing in certain products by conducting an internal review.

In a case before the Taipei District Court, the consumer filed a claim arguing that the sales representative of the bank was aware of the fact that the target product was substantially riskier than the products suitable for the plaintiff according to the suitability test, which was evidenced by the investment plan prepared by the sales representative.⁴¹ The court ruled that, even if the product at issue is not suitable for the consumer's risk-bearing ability, so long as the sales representative clearly explained the investment risks to the consumer and the consumer made his or her own decision to invest, the bank had sufficiently fulfilled its duty.

Similarly, in a case before the Taiwan High Court, the court also recognised that so long as the investor agreed to make such investment with written consent, the bank should be deemed to have fulfilled its duty to assess the investor's suitability with regard to such product.⁴²

36 Trust Law, Section 31.

37 See Taiwan High Court civil judgment 99-Zon-Shan-Zi-45 (2010).

38 See Taiwan High Court civil judgment 98-Zon-Shan-Zi-463 (2010).

39 See footnote 19, above, at 153–4.

40 Id. at 154.

41 See Taipei District Court civil judgment 99-Jin-Jian-Shan-Zi-5 (2010).

42 See Taiwan High Court civil judgment 98-Shan-Yi-Zi-1021 (2010).

In sum, the courts have generally held that the financial institutions have no obligation to actively refrain from selling financial products that are beyond a consumer's risk-bearing ability,⁴³ and generally yielded to the parties' freedom of contract.

With that said, for offshore structured products, the Securities and Futures Commission has promulgated the Regulations Governing Offshore Structured Products in 2009, pursuant to which financial institutions are prohibited from entering into transactions with non-professional investors regarding certain products and products beyond the investor's risk-bearing ability.⁴⁴ It should be noted that such regulations are still different from a general obligation to refrain from a transaction, and apply only to the transactions of offshore structured products.

Additionally, the courts sometimes make *de novo* decisions in evaluating an investor's suitability. However, in such cases, the courts rarely find an investor lacking suitability. For example, in one of the cases, the court ruled that so long as an investor has prior investment experiences in the stock market or the fund market, it is generally sufficient to conclude that such investor is suitable to invest in a structured bond.⁴⁵

iv Selling restrictions

The offering circulars of structured notes generally contain selling restrictions, including a clause stating that 'the Notes may not be sold or offered in the Republic of China ('R.O.C.') and may only be offered or sold to R.O.C. resident investors from outside Taiwan in such manner as in compliance with Taiwan securities laws and regulations applicable to such cross-border activities'.⁴⁶ Many investors relied on such language to claim that the financial institutions violated the selling restriction of specific products.

Most of the courts are of the view that the selling restriction should be construed as forbidding the notes from being sold or offered publicly and directly to Taiwanese investors. The common practice of the banks was to sell the structured notes through a specified monetary trust, in which the financial institutions are the direct investors and theoretically the products were not sold to the Taiwanese investors. From a legal point of view, the individual investors were the settlors of these trusts, instead of the direct investors of the structured notes. As such, the financial institutions did not violate such restriction of the offering circular under the investment structure through specified monetary trusts.⁴⁷

The minority view of the courts is that, in fact, such selling structure circumvented the selling restriction and should be deemed a violation of the offering circular.⁴⁸

v General consumer protection regulations

Prior to the enactment of the FCP Act in 2011, many investors raised claims pursuant to general consumer protection regulations, for example, the Consumer Protection Act

43 Chu, Te-fang, 'Should a selling institution refrain from transaction when a customer decides to purchase the financial product above one's risk level?', *Taiwan Law Journal*, 2011.4, at 196.

44 Regulations Governing Offshore Structured Products, Section 21.

45 See Taichung District Court civil judgment 98-Su-Zi-1060 (2009).

46 See Taipei District Court civil judgment 99-Su-Zi-438 (2010).

47 See Taiwan High Court civil judgment 99-Siao-Shan-Zi-5 (2010). See also Chen, Christopher Chao-hung, 'Structured notes fiasco in the courts: A study of relevant judgments between 2009 and 2010', *Academia Sinica Law Journal*, 2012.3, pp. 203-4.

48 See Taiwan High Court civil judgment 99-Zon-Shan-Zi-45 (2010).

and the relevant Civil Code provisions.⁴⁹ The vast majority of the courts overruled the consumer protection claims, stating that the purchase of structured products is generally for investment purpose and should not be governed by the general consumer protection laws.⁵⁰ The competent authority for consumer protection in Taiwan is also generally of the view that investment activities are highly risky and are different in nature from consumption activities. The application of general consumer protection laws should exclude structured financial product transactions.⁵¹ Since the promulgation of the FCP Act, it is expected that less investors will rely on general consumer protection regulations in financial and banking litigations when filing their claims.

V LIABILITY

In the discussion of liability calculation, the court is generally of the view that in the event that a financial institution is held liable for failing to fulfil the obligation of disclosure, thereby leading to cancellation of the contract, or that the contract was not effectively formed, the financial institution should return the full principal amount of investment.

Some financial institutions have asserted the causation defence, stating that since the damage of the investor was in fact caused by a *force majeure* event, namely, the global financial crisis, there was no proximate causation between the action of the financial institution and the damage of the investor. These financial institutions have claimed that even if the financial institutions fulfilled their obligation of disclosure, the investors would still make the same investment decisions and would still suffer from the global financial crisis. The courts remain split as to whether such defence of causation stands in such cases.⁵²

VI OUTLOOK AND CONCLUSIONS

Since the promulgation of the FCP Act, it can be expected that a majority of the disputes between financial institutions and investors and consumers will be resolved by the Financial Ombudsman Institution in future. Unlike the cases arising from structured product disputes, many of which are resolved through traditional litigation, since 2014 a certain proportion of the TRF investment disputes have been resolved through the mechanism of the Financial Ombudsman Institution. While the courts have provided abundant literature regarding structured product disputes, the TRF investment disputes that have been resolved through the Financial Ombudsman Institution have not been disclosed to the public, which means that, for the foreseeable future, it will be difficult to take a closer look at TRF or other investment disputes between consumers and financial institutions.

49 See footnote 47, above, at 207–8.

50 See Taiwan High Court civil judgment 99-Siao-Shan-Zi-5 (2010) (see footnote 47, above, at 208).

51 Consumer Protection Committee Letter Siao-Bao-Fa-Zi No. 0980010052.

52 See Taiwan High Court civil judgment 99-Zon-Shan-Zi-45 (2010). Contra Taipei District Court civil judgment 98-Su-Zi-1684 (2010).

UNITED KINGDOM

Christa Band and Jonathan Swil¹

I SIGNIFICANT RECENT CASES

There have been a number of important decisions of general application in the law of contract in the past year.

i Contractual formation and variation

In *Rock Advertising v. MWB Business Exchange Centre*,² the Supreme Court considered a ‘fundamental’ question: are ‘no oral variations’ clauses effective? The answer is yes.

The clause in question stated that: ‘All variations to this Licence must be agreed, set out in writing and signed on behalf of both parties before they take effect’. The licensee argued that there had been an oral variation to the payment obligations. The Supreme Court held (in agreement with the first instance judge, but overruling the Court of Appeal) that the oral variation was invalid. It gave effect to the contractual provision requiring specified formalities to be observed for a variation (subject to any subsequent estoppel) and reasoned that it would be contrary to ‘party autonomy’ if parties could not bind themselves as to the form of future variations. Full autonomy operates up to the point a contract is made, after which it is qualified in accordance with what the parties have agreed.

This is an important decision, and one that banks should find reassuring. The courts have promoted contractual certainty by giving effect to a common boilerplate clause.

ii Contractual interpretation – ‘reasonable endeavours’

*Astor Management v. Atalaya Mining*³ is another example of the courts’ willingness to uphold the parties’ bargain.

The defendants agreed to use ‘reasonable endeavours’ to obtain third-party debt funding, the attainment of which was a condition of their payment of the consideration for a copper mine. The funding was, in the event, obtained from the defendants’ parent company and the condition was not met, because it was not the particular type of funding required by the contract. While it might be difficult to prove breach of an endeavours clause (because the court will avoid second-guessing a party’s commercial judgement), that does not mean that no such obligation exists. The clause was given effect: the range of possible debt facilities that might satisfy the requirement did not render it uncertain, and there were objective criteria by which the reasonableness of the endeavours to obtain the facility could be assessed.

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2 [2018] UKSC 24; [2018] 2 WLR 1603.

3 *Astor Management AG v. Atalaya Mining Plc* [2017] EWHC 425 (Comm); [2018] 1 All ER (Comm).

iii Contractual interpretation – consent and discretion

Banks commonly have the right to withhold their consent to the exercise of a contractual right by their counterparty, provided it is not ‘unreasonable’ to do so. What does this mean?

In *Crowther v. Arbutnot Latham*,⁴ a secured lender refused consent for the sale of the property, in the absence of further security and a payment plan to cover a shortfall in the indebtedness that would be left following the sale. The lender’s refusal was held to be unreasonable. The purpose of the consent requirement was to preserve, rather than enhance, the lender’s original rights and it was known from the outset that the debt was not fully secured by the property. The refusal of consent, being aimed at seeking further security, was not based on the sale price and so was collateral to the purpose of the provision.

We also highlighted last year the courts’ approach to contractual discretions more generally. This issue arose again in *BHL v. Leumi ABL Ltd*.⁵ A discretion to set a fee of up to 15 per cent of the amounts collected by a bank for taking over a client’s collection of its receivables had to be exercised, given the wording of the contract, by reference to the cost the bank would incur in taking over the collections (and, following *Braganza v. BP Shipping Ltd*,⁶ not arbitrarily, capriciously or irrationally). It was not simply a licence to set a fee of 15 per cent if the bank so wished.

In *PAG v. RBS*,⁷ the Court of Appeal considered similar issues in the context of claims regarding its treatment by the bank’s restructuring group. This raised an issue as to the bank’s right to appoint a valuer that, at first instance, had been accepted as an ‘absolute right’ and thus not covered by authorities regarding the use of a discretion. The Court of Appeal disagreed with this categorisation and held that the power was one that needed to be exercised in pursuit of ‘legitimate commercial aims’, although on the facts it found these existed.

Where, however, the parties have specified a contractual standard of behaviour – as opposed to merely placing a discretion in one of their hands – English law will hold them to it. In *Lehman Brothers SPF v. NPC*,⁸ a decision in the derivatives context, the court considered the meaning of the requirement, under the 2002 ISDA Master Agreement, for a party, upon close-out, to use commercially reasonable procedures to determine the close-out amount with a view to reaching a commercially reasonable result. It held that these words required behaviour to meet objective standards set by the terms of contract, as opposed to ‘rationality’, and doubted whether this was a case of a ‘discretion’.

iv Contractual interpretation – terms

We noted in last year’s edition that in *Cavendish v. Makdessi*,⁹ the Supreme Court recrafted a more flexible, yet somewhat less certain, test for penalties. The lower courts appear to be applying the decision with some caution.

In *ZCCM Investments Holdings*,¹⁰ payment of instalments under a settlement agreement could be accelerated for breach, requiring the full amount to be paid within five business days, failing which, LIBOR plus 10 per cent interest would apply. This was not an unenforceable

4 [2018] EWHC 504 (Comm).

5 [2017] EWHC 1871 (QB); [2018] 1 All ER (Comm) 965.

6 [2015] UKSC 17; [2015] 1 WLR 1661.

7 *Property Alliance Group Ltd v. Royal Bank of Scotland Plc* [2018] EWCA Civ 355.

8 *Lehman Bros Special Financing Inc v. National Power Corp* [2018] EWHC 487 (Comm).

9 *Cavendish Square Holding BV v. Talal El Makdessi* [2015] UKSC 67; [2016] AC 1172.

10 *ZCCM Investments Holdings PLC v. Konkola Copper Mines Plc* [2017] EWHC 3288 (Comm).

penalty as the agreement was effectively a loan, the claimant had a legitimate interest in ensuring strict compliance and the interest rate was not extravagant because the same rate had been agreed for non-compliance with the primary payment obligation.

*Holyoake v. Candy*¹¹ is an illustration of the fact, should one be needed, that clauses that do not relate to a breach of contract – here a redemption sum on early repayment of a loan, extension fees and compounding interest – do not engage the rule on penalties.

v Damages for breach of contract

As an alternative to ‘ordinary’ compensatory damages, some claimants have been awarded ‘Wrotham Park’ damages.¹² The measure of these is what – hypothetically – the defendant would have been able to negotiate as a payment for release from the relevant obligation. The Supreme Court has provided some much-needed certainty as to when such damages (now to be called ‘negotiating damages’) will be available: following the breach of a contractual obligation that creates, or protects, an asset equivalent to a property right, rather than (the more usual case) where a contractual obligation creates a ‘commercial’ interest, damages for breach of which is to be measured in the usual way.¹³ This means non-compete and non-solicitation covenants, as ‘commercial’ interests, are not likely to attract these damages, whereas rights controlling the use of land, IP or confidential information more likely are. This decision applies a more principled and restrictive approach to damages of this kind than has hitherto been the case. But by clarifying matters, it may well encourage more parties to bring claims seeking such damages in future.

II RECENT LEGISLATIVE DEVELOPMENTS

The two most important legislative developments in the past year are the Criminal Finances Act 2017 and the General Data Protection Regulation (GDPR), which has been in force in EU Member States since 25 May 2018. The Criminal Finances Act 2017 has extended existing UK money-laundering and proceeds of crime legislation by introducing two new and potentially wide-reaching corporate criminal offences of failing to prevent the facilitation of tax evasion in the UK and overseas. The implications of this are highly significant for banks, which will need to have appropriate ‘prevention procedures’ in place, though this is outside the scope of this chapter.

No one can have failed to be aware of the GDPR. It includes a right for individuals to claim damages for a breach of their personal data protection rights, so time will tell whether its introduction will result in significant new claims against banks, particularly where there are any systemic or wide-scale breaches.

III CHANGES TO COURT PROCEDURE

New ‘umbrella branding’ for specialist higher civil courts in England and Wales came into effect on 2 October 2017. The Chancery Division (including the Bankruptcy and Companies Court, Patents Court and Intellectual Property Enterprise Court), certain Queens Bench

11 *Holyoake v. Candy* [2017] EWHC 3397 (Ch).

12 Named after the case in which they were first elucidated, *Wrotham Park Estate Co Ltd v. Parkside Homes Ltd* [1974] 1 WLR 789.

13 *Morris-Garner v. One Step Ltd* [2018] UKSC 20; [2018] 2 WLR 1353.

Division (QBD) courts (Commercial Court, Technology and Construction Court, Mercantile Court and Admiralty Court) and the Financial List (which straddles Chancery and QBD) are all now known under the collective name, 'the Business and Property Courts'. While not altering the work each court previously dealt with, the new 'branding' is intended to facilitate more flexible cross-deployment of judges and promote greater understanding of the work each court does.

At the time of writing, a two-year disclosure pilot scheme is under consideration in response to concerns over the cost, scale and complexity of disclosure in High Court litigation. If followed, the pilot would bring in a completely new set of rules for most cases in the Business and Property Courts and aim to foster a more collaborative and bespoke approach to disclosure. All court users, banks being no exception, will welcome any sensible simplification of the disclosure process, particularly if it leads to the speedier resolution of cases and reduces costs.

IV LEGAL PROFESSIONAL PRIVILEGE

Following last year's decision in *SFO v. ENRC*,¹⁴ there remains considerable debate over the limits of litigation privilege in the context of internal and regulatory investigations and the application of legal advice privilege to lawyers' notes of interviews with third parties (including employees). Banks will be watching keenly where this area of law goes next. Investigations remain a prominent feature of the regulatory environment, so the ability to rely on privilege where appropriate remains a key concern and requires careful thought in the planning of an investigation. Two recent cases suggest there is still (or is still a perception of) uncertainty in this area, but also illustrate that issues of privilege in this context will ultimately turn on the facts and the outcomes may not always be as strict as that in *ENRC*.

In *Bilta (UK) Limited v. RBS*,¹⁵ the issue was whether interview transcripts prepared during an internal investigation by a bank were created for the dominant purpose of litigation, and therefore protected by litigation privilege. The investigation followed a letter from HMRC indicating its view that an input tax could not be claimed and that penalties would potentially apply. It was conceded that at the time the transcripts were created, a claim in the First-tier Tribunal was reasonably in contemplation.

Relying on *ENRC*, the claimants argued that the investigation was merely aimed at persuading HMRC not to issue an assessment (i.e., that the transcripts were not created for the dominant purpose of litigation). The Court did not agree. Questions of dominant purpose turn on their facts so that conclusions reached in one case do not necessarily apply in another. The Court accepted that litigation was reasonably in contemplation because the HMRC letter was effectively a letter before claim and evidence of HMRC's enforcement activities and the overall context showed the high likelihood of an assessment by HMRC. So, the transcripts were created for the dominant purpose of litigation (and it did not matter, on the authority of *In re Highgrade Traders Ltd*,¹⁶ that once a dominant litigation purpose was established, there might also have been other, non-litigation purposes in play).

14 *Director of the Serious Fraud Office v. Eurasian Natural Resources Corporation Ltd* [2017] EWHC 1017 (QB); [2017] 1 WLR 4205. An appeal to the Court of Appeal is pending.

15 *Bilta (UK) Limited (In liquidation) v. RBS* [2017] EWHC 3535 (Ch).

16 [1984] BCLC 151.

Bilta reinforces the point that reasonable contemplation of litigation and dominant purpose will often be closely intertwined. More generally, it emphasises the importance of banks, and lawyers advising them, analysing very carefully the circumstances in which documents are created during an investigation to determine whether litigation privilege will be available – every case has its own facts and reported decisions are simply illustrations of the principles being applied to them.

*R v. SFO and XYZ*¹⁷ revisited the question of whether lawyers' notes of third-party conversations during an investigation can be protected by legal advice privilege. The documents under consideration were detailed, but not verbatim, notes of interviews with XYZ's executives, which led XYZ to self-report to the Serious Fraud Office (SFO). The judge considered the recent authorities, such as *ENRC*¹⁸ and *RBS*,¹⁹ in deciding whether privilege applied and criticised the SFO's acceptance of the material as privileged. In doing so, he expressed the trenchant view that the case law on interview notes is clear. In reading this decision, however, some care is needed. The judge did not expressly refer to the fact that the case involved interview notes with third parties in the legal advice privilege context. If litigation privilege is available matters will be different.

Another part of the judgment of interest is the judge's acceptance of a submission that parts of the notes containing advice or lawyers' impressions could be redacted. By contrast, in *ENRC*, the court spoke of notes *in toto* being privileged to the extent that they betrayed the 'trend' of legal advice. Thus, to the extent that such notes evidence such material, the question of whether it is the whole or only part of the document that can be withheld ultimately will turn on the degree of 'severability' of any legal advice or 'impressions' in the note from the remainder of the document.

Another case of interest in the sphere of legal professional privilege is *R v. Jukes*.²⁰ This concerned litigation privilege in the criminal context. In it, the Court of Appeal endorsed the view that, in that context, the relevant 'litigation' is the criminal prosecution itself – not the preceding investigation.

Often, a pragmatic approach has to be taken to the preservation of privilege in an investigation: the bank has choices and a balance has to be struck between gathering information and recording it in a way that makes it useful to the bank and its advisers and the preservation of privilege to the fullest extent possible with the practical limitations that this may put on the investigation.

V JURISDICTION AND CONFLICTS OF LAW

i Cross-border garnishment

Banks commonly operate in foreign jurisdictions through local 'branches' of a single legal entity registered in their home jurisdiction.

*Republic of Kazakhstan v. Bank of New York Mellon (London Branch)*²¹ (BNYM) is a reminder that international banks caught up in their customers' disputes can find themselves

17 [2018] EWHC 856.

18 *Director of the Serious Fraud Office v. Eurasian Natural Resources Corporation Ltd* [2017] EWHC 1017 (QB).

19 *Property Alliance Group Ltd v. Royal Bank of Scotland Plc* [2015] EWHC 3187 (Ch); [2016] 1 WLR 992.

20 [2018] EWCA Crim 176.

21 *National Bank of Kazakhstan and The Republic of Kazakhstan v. The Bank of New York Mellon* [2017] EWHC 3512 (Comm).

simultaneously exposed to the potentially conflicting effects of the laws of the different jurisdictions in which they operate. They may need to ensure their customer contracts are drafted to make abundantly clear who bears the risk of such conflict and consider operating in jurisdictions calculated to limit the risk of conflicts arising at all. Here, a third party was seeking enforcement of a US\$500 million arbitral award against the global assets of the Republic of Kazakhstan. The bank, a Belgian-registered entity, was served with Belgian and Dutch orders garnishing assets comprising Kazakhstan's sovereign wealth fund. BNYM held, in total, US\$22 billion of the fund's cash and securities as custodian for the National Bank of Kazakhstan (NBK) under a global custody agreement (GCA) and froze all of them, on the basis the effect of the Belgian order was (unlike the effect of equivalent orders under English and many other laws) expressed to apply to all assets BNYM held for the sovereign wealth fund, wherever they may be considered to be located, and notwithstanding that they greatly exceeded the value of the arbitral award. Non-compliance with the Belgian and Dutch orders could have led to criminal and civil liability for the bank.

Kazakhstan and NBK sought declarations in the English Court to the effect that BNYM was not entitled to freeze the assets under the GCA, principally because the assets were said to be located at the London branch and the Belgian and Dutch orders were not, as a matter of English conflicts law, recognisable in England.

The Court's focus was on a *force majeure* clause in the GCA, which was expressed to excuse any non-performance (in this case, the failure to follow NBK's instructions) caused by any order imposed by any judicial authority. The Court interpreted this broadly and held that it covered the Belgian and Dutch orders (provided the necessary causative link was established) and was not, as NBK argued, limited to orders recognised by the English Court. On that basis, the claim was dismissed.

The Court gave the contractual words their plain meaning, and the decision is encouraging for banks in relation to the effect that will be given to similar *force majeure* clauses in custody agreements.²²

*Taurus Petroleum Ltd v. State Oil Marketing Company*²³ also involved enforcement of a foreign arbitral award against an asset held by the local branch of a foreign bank, this time letters of credit (LoCs) issued by the London branch of a French bank. The Supreme Court had to decide where the *situs* of the debt owed under the LoC was in order to determine whether an English third-party debt order against the LoC could be made. On the basis of Article 3 of the Uniform Customs and Practice for Documentary Credits, the Court accepted that branches of banks in different countries are treated as separate banks for the purpose of LoCs and therefore that the sole residence of the debtor bank was London. Applying the general rule that debts are situated in the place of the debtor's residence, it concluded that the *situs* of the LoC was England. In doing so, the Supreme Court overruled the Court of Appeal's decision in *Power Curber v. National Bank of Kuwait*,²⁴ which held that debts due under LoCs are located in the place of payment.

22 The decision and the Court's reasoning were upheld on appeal: *National Bank of Kazakhstan v. The Bank of New York Mellon SA/NV London Branch* [2018] EWCA Civ 1390.

23 *Taurus Petroleum Limited v. State Oil Marketing Company of the Ministry of Oil, Iraq* [2017] UKSC 64; [2017] 2 WLR 1170.

24 *Power Curber International Ltd v. National Bank of Kuwait SAK* [1981] 1 WLR 1233.

ii Immobilised securities

Most securities are held by custodians in ‘immobilised’ form with central depositories. Investors trade interests in the securities held through a chain of counterparties that are ultimately recorded as book entries in clearing systems. Questions that frequently arise are what rights investors have in respect of such securities and what law governs them.

In *Secure Capital SA v. Credit Suisse*,²⁵ an investor’s claim against the issuer of notes was based on breach of a contractual term of the notes, which were governed by English law. The identity of the parties entitled to sue under a contract is, under English conflicts law, to be determined by the law of the contract. Therefore, under their terms, only the bearer (BNYM) could sue on the notes.

To avoid this conclusion, the investor argued that in the case of immobilised securities, the law of the clearing system should determine who could sue on the notes because there would otherwise be no one capable of claiming damages against the issuer. This was rejected.

iii Islamic finance

Major Islamic financing arrangements have become increasingly prominent in recent years. They can be constituted by several documents with different applicable laws. *In re Dana Gas*²⁶ provides reassurance that the governing law of particular documents will in general be respected by the English courts, whatever the effect of other laws involved. The terms of a purchase undertaking governed by English law was said to be inconsistent with shariah law principles and therefore unlawful under UAE law. Under the Rome I Regulation,²⁷ questions of the validity of a contract are determined by its governing law. The fact that it might be invalid under a foreign law is irrelevant (save to the extent that limited exceptions under that Regulation provide otherwise). Accordingly, the purchase undertaking was enforceable.

VI SOURCES OF LITIGATION

i Loan repayment

The enforcement of loan and security agreements is a common source of banking litigation. A few recent cases show the courts’ preparedness to enforce such agreements on their terms in favour of banks and that various legal doctrines, such as implied terms and estoppel, are relied on, often unsuccessfully, by borrowers, to try to get around this.

A bank’s omission was relied on in *General Mediterranean Holding SA v. Qucomhops Holdings*²⁸ to resist repayment. The lender failed to preserve its security in foreign insolvency proceedings and as a result, fraudsters made off with the only assets available to the borrowers to repay the loan. The borrowers argued that the lender was under a duty to preserve the security and by not doing so, their repayment obligation was discharged. The judge made clear that the lender has to be under an express duty to take a step where the failure to do so is relied upon to discharge the repayment obligation. The default position is that creditors are

25 [2017] EWCA Civ 1486.

26 [2017] EWHC 2928 (Comm).

27 Regulation (EC) No. 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I).

28 *General Mediterranean Holding SA SPF v. Qucomhops Holdings Ltd* [2017] EWHC 1409 (QB).

under no duty to take any steps to preserve their security.²⁹ In this case, no such duty could be implied as a matter of law or equity and (relying on *Marks & Spencer*³⁰) it was not necessary to imply it as a matter of fact.

By contrast, there was no question that the bank had a right to be repaid in *Clydesdale Bank plc v. Gough*.³¹ Rather, the issue was whether the bank was estopped by an alleged promise to allow the defendant to sell his assets to reduce his indebtedness before it enforced the loan. On the evidence, there was no clear and unequivocal promise or common understanding that the bank would not enforce its strict rights at the time the loan was entered. The loan was governed by a written contract and the bank was entitled to repayment and possession.

ii LIBOR claims

In its high-profile decision in *PAG v. RBS*,³² the Court of Appeal dismissed a number of claims against the defendant bank arising from the sale of interest rate swaps to the claimant, and its alleged manipulation of LIBOR. In respect of specific LIBOR-related issues, the Court of Appeal's judgment is perhaps most notable for its acceptance of the claimants' position that the defendant's proffering of the swaps could be conduct from which an implied representation as to its conduct in relation to LIBOR could be drawn – although the Court of Appeal agreed that there was no evidence of such manipulation.

iii Mis-selling, and duties of care

We noted in last year's edition the prevalence of banks' potential liability for mis-selling claims and the extent to which customers are seeking to invoke duties owed by banks in the context of advice they are alleged to have been given. This theme continues in relation to 'mezzanine duties'. Claims under Section 138D of the Financial Services and Markets Act 2000 (FSMA) have also come before the courts.

In *Marz v. Bank of Scotland*,³³ it was a condition of the claimant's loan that it enter into an interest rate swap. The claimant alleged a contractual duty by the bank to ensure the swap was suitable and tortious duties to advise it correctly and explain its options to enable it to make an informed choice – the mezzanine or 'intermediate' duty.

The contractual duty was rejected on the basis of a no-reliance clause in an ISDA Master Agreement. The facts also did not support an advisory duty – the claimant had its own advisers and did not rely on the bank. As to the intermediate duty, the judge commented that this was effectively part of the wider question of whether there was an advisory relationship and associated duties. Therefore, it was also rejected on the basis of the finding that the bank was not acting as an adviser or alternatively, the no-reliance clause. The latter was also found not to be an exclusion clause and so was not subject to the reasonableness test in the Unfair Contract Terms Act 1977 (UCTA), but even if it was, it was reasonable.

In *PAG v. RBS*, discussed above, one of the claims against the bank involved similar allegations in relation to an interest rate swap. In this case, the Court of Appeal also steered

29 *China & South Seas Bank v. Tan* [1990] 1 AC 536; [1990] 2 WLR 56.

30 *Marks & Spencer Plc v. BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2016] AC 742.

31 [2017] EWHC 2230 (Ch).

32 [2018] EWCA Civ 355.

33 [2017] EWHC 3618 (Ch).

away from talk of an intermediate or mezzanine duty. In its view it saw this expression as unhelpful, preferring to stress that the existence (or otherwise) of a duty of care, and its extent, is an assessment of whether, on the facts, responsibility has been assumed.

Claims for damages by private persons under Section 138D(2) of the FSMA for a firm's breach of rules made by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority are not common and do not often succeed. However, the claim in *Abdullah v. Credit Suisse*³⁴ did.

The claimants, a wealthy Kuwaiti family, had entered into various structured capital-at-risk products at the bank's recommendation. Following a restructuring of their portfolio recommended by the bank, they subsequently decided not to meet a margin call, which resulted in them losing their investment. It was claimed that the bank had breached various aspects of the Conduct of Business (COBS) Rules. That claim succeeded on the basis that the claimants' willingness to invest in the structured products was predicated on the bank's assessment that it was unlikely that there would be a margin call and so the products matched their risk appetite.

Another Section 138D claim for breach of various COBS rules in connection with the sale of swaps was rejected in *Parmar v. Barclays Bank*.³⁵ Interestingly, the judge commented that, had breaches been established, the bank would not have been entitled to rely on clauses in the customer's contract, stating the basis of the parties' relationship (known as 'basis clauses'). This was because COBS Rule 2.1.2 was engaged in this case, preventing any exclusion or restriction of the bank's Section 138D(2) liability.

It is likely that there are fewer Section 138D claims because of the FCA's requirement in recent years that banks institute review and redress schemes in relation to their selling of interest rate hedging products prior to the financial crisis. This is usually done by the appointment of an independent 'skilled person' under Section 166 of the FSMA. Claimants disappointed by the outcomes of such schemes have brought claims impugning the way in which they have been conducted, to try to obtain redress a different way.

While there have been conflicting decisions in this area, welcome clarification has now come in *CGL Group Ltd v. Royal Bank of Scotland*.³⁶ The Court of Appeal concluded that banks do not owe a duty of care to claimants to conduct reviews with due skill and care. It would be unusual for the common law to impose a common law duty on a statutory framework; the reviews are not, in truth, voluntary; it would be surprising for the bank to owe a duty where the independent reviewer does not, and it would allow time-barred claims to be litigated via the 'back door'.

Another duty of care case that has garnered much attention, this time in an Islamic finance context, is *Golden Belt 1 Sukuk v. BNP Paribas*.³⁷ The question was whether a bank, as arranger of shariah-compliant certificates, owed investors a duty of care in relation to the execution of Saudi law-governed promissory notes (which required handwritten signatures). A duty was owed, and breached, by the bank's failure to follow legal advice as to the steps required to execute shariah documents.

34 *Abdullah v. Credit Suisse (UK) Ltd* [2017] EWHC 3016 (Comm).

35 [2018] EWHC 1027 (Ch).

36 *CGL Group Limited v. The Royal Bank of Scotland Plc & National Westminster Bank plc* [2017] EWCA Civ 1073; [2018] 1 WLR 2137.

37 *Golden Belt 1 Sukuk Company BSC (C) v. BNP Paribas; FCOF II UB Securities LLC v. BNP Paribas* [2017] EWHC 3182 (Comm); [2018] 1 All ER (Comm) 1126.

iv Facilitating fraud

The Court of Appeal has upheld the decision in the *Singularis* case.³⁸ As mentioned in last year's edition, at first instance, a bank was found negligent and in breach of contract for failing to make proper enquiry and stop payments that it knew or ought to have known were being effected fraudulently (based on the duty in *Barclays Bank plc v. Quincecare Ltd*³⁹). The appeal was dismissed effectively on two grounds: an illegality defence was unsuccessful because despite being a director of the account holder, the fraudster's conduct could not be attributed to it and it did not matter that only creditors of the account holder (which was in liquidation) would benefit in practice from the application of the *Quincecare* duty. The issues on appeal confirm that the case turns on its unusual facts.

Any principle of broader application that would require banks to monitor closely for fraud and stop payments on all of their customer accounts would place a heavy burden on them indeed.

This is demonstrated to some extent by *Chudley v. Clydesdale Bank*.⁴⁰ Investors paid money to a fraudulent company that held an account with the bank from which the bank had (wrongly) permitted payments to be made. The bank also signed letters used by the fraudsters to induce the investments. However, there was insufficient proximity between the bank and the investors to support a duty of care, the relevant bank employee was foolish, but not a dishonest assistant, and there was no restitutionary claim because the statements had not been relied on and the bank was not enriched because it owed a corresponding liability to its customer.

VII EXCLUSION OF LIABILITY

We discussed in last year's edition the importance for banks of exclusion clauses and the distinction between them and basis clauses. Two recent banking cases continue to highlight this.

A party relying on an exclusion clause in its standard terms of business needs to satisfy the reasonableness test in the UCTA. In a decision of some significance,⁴¹ the Court of Appeal has shed light on what it means for commonly used sets of terms to be 'standard'. It held that an industry-wide set of terms (in this case, a Loan Market Association (LMA) syndicated facility) are not the party's standard terms if they are not used by that party habitually. Even if they are, they are unlikely to be 'standard' in a particular case if more than insubstantial variations are negotiated. The Court left for another day the question of whether habitually used LMA terms on which a party refuses to negotiate any amendments are its standard terms (although it hinted they may well be).

The important decision of *First Tower Trustees v. CDS Ltd*⁴² concerned a claim for misrepresentation in the context of a lease of warehouse premises. The landlord had made a misrepresentation in its replies to pre-contractual enquiries but the lease contained a

38 *Singularis Holdings Ltd (in official liquidation) v. Daiwa Capital Markets Europe Ltd* [2018] EWCA Civ 84; [2018] 1 WLR 2777.

39 [1992] 4 All ER 363.

40 [2017] EWHC 2177 (Comm).

41 *African Export-Import Bank v. Shebah Exploration & Production Company Limited* [2017] EWCA Civ 845; [2018] 1 WLR 487.

42 [2018] EWCA Civ 1396.

provision to the effect that the tenant acknowledged that it had not relied on any statements or representations by the landlord in entering into the lease. The Court of Appeal held, contrary to the approach adopted in previous cases, that a clause of this nature – which on the fact of it raised a contractual estoppel against an argument of misrepresentation – could be regarded as an exclusion of liability and so subject to Section 3 of the Misrepresentation Act 1967 (which subjects exclusions of liability for misrepresentation to a reasonableness test). This was because the effect of such a clause was to negate liability, which, if the clause had not been there, would have existed.

An important part of the Court of Appeal's judgment was its examination of the distinction between provisions that, correctly interpreted, (1) raise a contractual estoppel against arguments of liability arising within the parties' relationship, and (2) truly define the primary scope of the relationship to begin with. The Court of Appeal observed that past cases on contractual estoppel tended to conflate clauses within the first category with those in the second. However, the issues need to be kept distinct because, if within the first, a clause could properly be seen as exclusionary and so subject to any relevant controls, such as Section 3 of the Misrepresentation Act. By contrast, provisions within the second category determine what the scope of the primary obligations are to begin with, which is a question of construction.

VIII LOOKING AHEAD

i Brexit

Last year, we discussed two issues concerning the impact of Brexit on litigation:

- a What will the differences on jurisdiction and applicable law be in a post-Brexit world?
- b Are there issues that arise from the transitional period?

Unfortunately, uncertainty surrounding these issues continues. Under negotiation at the time of writing is the draft agreement for the withdrawal of the UK from the EU. It was hoped that this may mitigate some uncertainty, in particular, in the field of jurisdiction, and recognition and enforcement of judgments, by providing for transitional provisions. In June 2018, the UK and EU27 negotiators unveiled, in a joint statement, their agreed position on this point. In short, the position they reached was that, in situations involving the UK, the Brussels I Recast would continue to apply where proceedings had been commenced before the end of the general transition period contemplated by the draft withdrawal agreement (anticipated to be 31 December 2020).

Of course, whether the withdrawal agreement is actually agreed and implemented is, at the time of writing, itself uncertain but, putting that to one side, there are some positive aspects to this proposal. It makes sense that the *status quo* is preserved indefinitely for proceedings commenced before the end of the transition period. However, the lack of any specific provision for cases involving a jurisdiction clause in favour of the English courts entered into prior to the end of the transition period was a missed opportunity. That omission means that, even if the withdrawal agreement is implemented, parties will likely need to continue, for the foreseeable future, to make more rounded assessments of their use of English jurisdiction clauses (in particular, in circumstances where enforcement of a resultant judgment is likely to be required in territories where enforcement of an English judgment currently enjoys the benefit of EU legislation).

Any further agreements with the EU regarding English jurisdiction clauses and judgments would appear to have to await an agreement, if any, that the UK manages to conclude in this sphere as part of its future relationship with the EU (which, at the time of writing, has not been progressed). Given the proposed terms of the withdrawal agreement, it is clear that such an agreement would also, assuming that the withdrawal agreement is implemented, be important to avoid a wave of pre-emptive litigation before the run-off period in any withdrawal agreement ends.

ii Cases to watch

The pending appeal in *SFO v. ENRC*⁴³ is one for all litigators to watch out for. It is hoped the decision will provide much-needed clarity as to the ability to rely on regulatory investigations for the purpose of litigation privilege and the status of documents created during them, and the extent to which interview notes are protected.

An attempt by the defendant to apply for summary judgment in *Andric v. Credit Suisse (UK) Ltd*⁴⁴ has been dismissed in the High Court. The trial will touch upon the obligations of banks and their employees to avoid false representations to customers.

43 *Director of the Serious Fraud Office v. Eurasian Natural Resources Corporation Ltd* [2017] EWHC 1017 (QB); [2017] 1 WLR 4205.

44 [2017] EWHC 1724 (Comm).

UNITED STATES

*Jonathan I Blackman, Pascale Bibi and Jessa I DeGroot*¹

I OVERVIEW

The United States continues to be an active forum for banking-related litigation. Financial institutions continue to experience litigation exposure to financial product-related suits, as well as antitrust and other claims arising out of an active regulatory investigation landscape. Litigation derived from international sanctions violations has also been on the rise, though a recent ruling that claims against foreign corporations, including foreign banks, cannot proceed under the Alien Tort Statute may hinder future claims of this kind by private civil plaintiffs. Banks must continue to be attuned to privilege laws in multiple jurisdictions to guard against the potential disclosure of confidential information in private litigation in the United States. In addition, the recent passage of the Clarifying Lawful Overseas Use of Data (CLOUD) Act also raises questions regarding the protection of data located abroad in US litigation, though the practical effects of the law remain to be seen.

Though much of the litigation arising out of the foreign exchange (FX) market regulatory investigations has settled, including antitrust class actions, new suits have been filed based on investigations in other markets. Courts have heightened the requirements for actions to proceed on a class-wide basis by implying additional requirements into the class certification rule, which curbs class actions and the accompanying settlement pressures. In addition, Congress nullified a proposed rule promulgated by the Consumer Financial Protection Bureau (CFPB) prohibiting the use of class action waivers in arbitration agreements, which continues to be a method widely used by financial institutions to control dispute resolution arising out of consumer contracts and limit exposure to costly class actions. The government has also taken actions to begin a rollback of rules promulgated pursuant to the Dodd-Frank Wall Street Reforms Act (Dodd-Frank), including by amending Dodd-Frank to narrow its application. That rollback has been accompanied by the most significant drop in regulatory rulemaking since the collection of such data began in the 1970s. Nonetheless, as in many other areas, it remains to be seen what effect these actions will have in the banking litigation sphere.

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II LEGISLATION

i The federal system

The United States legal system is divided into federal and state jurisdictions. The federal government consists of three branches: legislative, executive and judicial. The majority of regulators that oversee financial matters (e.g., the Department of Justice, the Federal Reserve, and the Securities and Exchange Commission) are parts of the federal government, broadly defined, although states also have their own bank regulatory regimes.

The federal government and the state governments are considered to be separate sovereignties, and, accordingly, have concurrent legal regimes. Each of the 50 states has an independent court system and its own body of law. As a result, banks are subject to both federal and state law, which apply with equal force, but may differ in their requirements, with federal law taking precedence where applicable. Some states take a particularly active role in bank regulation; for example, as would be expected, New York and its Department of Financial Services maintain a dynamic presence in US banking regulation, and would be expected to continue to do so even if there were to be a decrease in activity by federal agencies.

ii Recent legislation

Significant banking legislation, the Economic Growth, Regulatory Relief and Consumer Protection Act (S.2155), has been recently enacted by the Trump administration. S.2155 significantly revises Dodd-Frank and the Consumer Protection Act of 2010 in an effort to reduce the burden on small to medium-sized banks and bank holding companies. It does so by limiting the application of Dodd-Frank's enhanced prudential standards to banks with US\$250 billion or more in global assets as compared with the current US\$50 billion threshold, and by exempting holding companies with US\$10 billion or less in global assets from certain requirements and rules, including the Volcker Rule, which, among other things, prohibits banks from making certain investments with their own funds and from making certain speculative investments. The impact of S.2155 will depend heavily on its implementation by the Federal Reserve and other bank regulators, especially the Office of the Comptroller of the Currency (OCC) and the Federal Deposit Insurance Corporation. In addition, the Federal Reserve, as well as other bank regulators, are expected to propose changes to relax the Volcker Rule later this year, which will likely allow banks to engage in a wider range of trading.

At the state level, little legislative activity has occurred in recent months, which is generally attributable to the secondary role of the states in banking regulation. The state of New York, however, has implemented new cybersecurity regulations that apply to companies operating under New York banking, insurance or financial services laws. Those regulations generally require the development of cybersecurity programmes and policies, limitations on access to data systems, use of qualified personnel, preparation of an incident response plan, and notification of the New York State Department of Financial Services within 72 hours of a cybersecurity event. These requirements, and the increase in cybersecurity attacks generally, will likely result in increased litigation in this area for banks that experience such attacks. Cybersecurity attacks, however, can also result in banks becoming plaintiffs when the banks' customers information is compromised as a result of cybersecurity attacks on third parties.²

2 *First Choice Federal Credit Union v. the Wendy's Co.*, No. CV 16-506, 2017 WL 1190500, at *1 (W.D. Pa. 31 March 2017) (upholding decision by Magistrate Judge denying Wendy's motion to dismiss claims brought by banks for breach of customers' credit and debit card information).

III JURISDICTIONAL MATTERS

In the United States, personal jurisdiction – or the power of a particular court to hale in an entity to answer for a claim – is either general, meaning that a court can hear any claim against that entity, or specific, meaning that the court can hear only claims ‘arising out of or related to the defendant’s contacts with the forum’.³

i General personal jurisdiction

Traditionally, courts were permitted to exercise general personal jurisdiction over an entity with ‘systematic and continuous contacts’ to the state where the court was located, which, in practice, meant that foreign banks were routinely subject to suit wherever they had a branch or representative office, subject only to discretionary rules of *forum non conveniens*. In 2014, the Supreme Court substantially limited the power of the US courts over foreign entities in *Daimler AG v. Bauman*,⁴ ruling that general personal jurisdiction could only be exercised over a company if the forum court is within the company’s state of incorporation, or the state of the company’s principal place of business, absent exceptional circumstances.⁵ Since *Daimler*, the Supreme Court has made clear that the defendant must truly be ‘at home’ in the forum state for general personal jurisdiction to exist.⁶ While *Daimler* has spawned much litigation, plaintiffs have been unsuccessful in articulating ‘an exceptional case’ in which the defendant’s operations were so substantial and of such a nature that would warrant deviation from this rule, and even the presence of 2,000 miles of railroad and over 2,000 employees in a US state was held to be not enough to support general jurisdiction when the suit was unrelated to any of that in-state activity.⁷ Thus, the majority of US courts now do not have general personal jurisdiction over foreign banks that are not incorporated in the United States and do not have their headquarters there.⁸

Plaintiffs have sought to avoid the impact of *Daimler* by advancing theories based on consent to jurisdiction – specifically by arguing that obtaining a business licence to operate within a state, as banks must to operate a local branch, should constitute consent to general jurisdiction there. States have issued conflicting opinions on this point.⁹ In New York, courts

3 *Helicopteros Nacionales de Colombia, S.A. v. Hall*, 466 U.S. 408, 415 No. 9 (1984).

4 571 U.S. 117 (2014).

5 *Daimler AG*, 571 U.S., 136.

6 *Daimler AG*, 571 U.S., 138 No. 18.

7 *BNSF Ry. Co. v. Tyrrell*, 137 S. Ct. 1549 (2017).

8 See, e.g., *Brown v. Lockheed Martin Corp.*, 814 F.3d 619, 628-29 (2d Cir. 2016) (refusing to find an exceptional case where the defendant maintained a physical presence in the US state for over 30 years, ran operations out of that state and employed 70 workers there, and generated substantial revenue from its operations there); *Nypl v. JPMorgan Chase & Co.*, 15-CIV-9300 (LGS), 2018 WL 1472506, at *4 (S.D.N.Y. 22 March 2018) (refusing to find an ‘exceptional case’ for general jurisdiction based on foreign banks’ participation in criminal proceedings in the US and advertisements accessible to consumers in the US).

9 For example, courts in Delaware issued split decisions on whether registration operated as consent, before the Delaware Supreme Court – the state’s highest court, and the final arbiter of Delaware state law – ruled that registration did not function as consent. *Genuine Parts Co. v. Cepec*, 137 A.3d 123, 148 (Del. 2016).

have not determined whether a licence to do business in the state will function as consent to personal jurisdiction, and legislation is pending to impose this requirement.¹⁰ At the time of writing, this question remains unresolved.

ii Specific personal jurisdiction

Plaintiffs have also sought to compensate for the loss of general jurisdiction in cases where it would previously have existed as a matter of course by broader assertions of specific jurisdiction, which requires that the claims arise out of the defendants' forum-related contacts, arguing that their suits 'arise out of or relate to' what are sometimes relatively minimal actions by the defendant company within the forum.¹¹ This strategy was envisioned by the *Daimler* court itself, which noted that 'specific jurisdiction has become the centrepiece of modern jurisdiction theory'.¹² Specific jurisdiction can be heavily fact-dependent and, while some courts require that the in-forum conduct be the proximate cause of the injury, other courts only require the in-forum conduct to be a but-for cause.¹³ Under either approach, the injury to the plaintiff must have a connection to the defendant's conduct within the forum, thereby providing a causal constraint on the use of specific jurisdiction. Thus, specific personal jurisdiction often exists where the injury to the plaintiff arises out of conduct taken in, or purposefully directed to, the United States.¹⁴

One area that has spurred particularly interesting litigation is banks' use of correspondent bank accounts in New York to clear dollar transactions within the state. In New York, those accounts can provide a basis for specific personal jurisdiction, but only where clearing transactions form part of the plaintiff's claim and the bank knowingly made use of the correspondent account (i.e., the bank acted with knowledge of the nature of the underlying transaction for which the correspondent account is used to move dollars as payment).¹⁵ This area of law continues to evolve, as courts grapple with the extent to which routine banking contacts, such as use of New York correspondent accounts, are sufficient to create specific jurisdiction over otherwise non-US-related claims.

10 N.Y. State Assembly, A6714, Reg. Sess. (N.Y. 2015), http://assembly.state.ny.us/leg/?default_fld=%0D%0A&bn=A6714&term=2015&Summary=Y&Actions=Y&Votes=Y&Memo=Y&Text=Y.

11 Much of the increase in specific personal jurisdiction litigation has centered on products liability and non-bank commercial activity-based jurisdictional fact patterns. See, e.g., *Bristol-Myers Squibb Co. v. Super. Ct. of Cal.*, 137 S. Ct. 1773 (2017).

12 *Daimler AG*, 571 U.S., 128 (citation omitted) (internal quotation marks omitted).

13 *SPV Osus v. UBS AG*, 882 F.3d 333, 334 (2d Cir. 2018).

14 *Charles Schwab Corp. v. Bank of Am. Corp.*, 883 F.3d 68, 81-88 (2d Cir. 2018) (finding that personal jurisdiction exists for claims arising out of transactions in the US, but not for claims arising out of conduct undertaken abroad); see also *Nypl.*, 2018 WL 1472506, at *5-6 (finding specific personal jurisdiction where the alleged injuries arose out of conduct for which the banks entered guilty pleas with the US Department of Justice admitting to actions directed at or occurring in US states, but refusing to extend that jurisdiction to foreign parent holding companies).

15 *Rushaid v. Pictet & Cie*, 28 N.Y.3d 316, 338 (2016), reh'g denied, 28 N.Y.3d 1161 (2017); see also *Licci ex rel Licci v. Lebanese Canadian Bank*, SAL, 732 F.3d 161, 171 (2d Cir. 2013).

IV PROCEDURAL ISSUES

i Injunctions and attachment

Banks will frequently encounter asset freezing orders – injunctions or attachment orders requiring restraint of assets held by the bank – in connection with litigation to which the bank is not a party. There is variation among US jurisdictions as to the extent of a financial institution's obligation to freeze assets held outside the United States in response to such orders. In New York, for example, the 'separate entity rule' allows New York courts to freeze only those assets located within the United States.¹⁶

With regard to post-judgment execution on assets or injunctions in aid of such execution, recent changes to personal jurisdiction law, discussed in greater detail in Section III, above, have limited the power of US courts to enforce such orders against non-parties for assets located outside the forum. Following the *Daimler* decision, 'a court can enforce an injunction against a nonparty [bank] only if it has personal jurisdiction over that nonparty'.¹⁷ Even if personal jurisdiction exists, financial institutions may still raise principles of international comity as a further defence, particularly when the bank is a non-party that would not expect US law to apply.¹⁸ Thus, financial institutions wishing to resist the enforcement of third-party enforcement orders, now may be able to assert a personal jurisdiction defence that was not available before *Daimler*, in addition to the traditional defence of comity.

ii Class actions

Financial institutions will frequently encounter litigation in the form of a class action brought on behalf of numerous plaintiffs. Under Federal Rule of Civil Procedure Rule 23, which governs class actions in federal court, plaintiffs must affirmatively demonstrate several requirements: numerosity of parties, commonality of questions of law or fact, typicality of the representative plaintiffs' claims relative to the class, and fair and adequate representation of the class. In addition, courts have interpreted Rule 23 to contain an implicit 'ascertainability' requirement, meaning that the members of the proposed class must be readily identifiable based on objective criteria that will not require individual determination.¹⁹ At least one court has taken that requirement even further by requiring that the class claims be administratively feasible as well.²⁰ Such requirements provide an additional, useful basis for banks to defeat plaintiffs' use of a class action in instances where the individuals allegedly harmed, or the harm itself is difficult to define.

To maintain a class action, the court must affirmatively approve of the class by 'certifying' it pursuant to Rule 23. In many cases, class certification, by magnifying the defendants' potential exposure, helps drive settlement. Settlements of class actions after certification must be approved by the court upon a finding that the settlement is fair, reasonable and adequate.

16 *Motorola Credit Corp. v. Standard Chartered Bank*, 24 N.Y.3d 149, 156 (2014).

17 *Gucci Am., Inc. v. Weixing Li*, 768 F.3d 122, 134 (2d Cir. 2014) (emphasis added).

18 *Id.* at 138-42; see also *Peterson v. Islamic Republic of Iran*, 876 F.3d 63, 94 No. 23 (2d Cir. 2017).

19 See, e.g., *In re Petrobras Secs.*, 862 F.3d 250, 264-65 (2d Cir. 2017); *Sandusky Wellness Ctr., LLC v. Medtox Sci., Inc.*, 821 F.3d 992, 995 (8th Cir. 2016).

20 *Byrd v. Aaron's Inc.*, 784 F.3d 154, 162-63 (3d Cir. 2015).

iii Choice of law

Choice of law considerations within the United States can be particularly complex, and even more so in cases involving global banks, as courts must decide whether to use foreign, federal or state law – and if state law is applicable, which of the 50 states' laws will apply. Different US jurisdictions apply different tests to resolve choice of law questions, in some instances looking to which body of law bears the most 'significant relationship' to the suit, while in other instances rigidly applying formulas that require, for example, a contract dispute to be adjudicated under the law of the place where the contract was formed.

V PRIVILEGE AND DISCLOSURE

i Bank examination privilege

In the United States, banks benefit from a privilege protection for confidential information shared with their bank regulators, known as the bank examination privilege. Banks are heavily regulated by a patchwork of state and federal agencies, which frequently obtain confidential information related to a bank's operations and performance in the exercise of their oversight duties. Such confidential information is often sought in litigation by third parties against banks, and the bank examination privilege may be used to protect this information from disclosure.

The bank examination privilege belongs to the regulatory agency. It is up to the bank and its outside counsel to preserve the privilege when responding to subpoenas or discovery requests for documents covered by the privilege. Documents covered by the privilege should not be produced in parallel private litigation or to requests from non-banking agencies, unless the privilege has been waived by the applicable regulator or production has been ordered by a court following its review. In practice, outside counsel should notify the regulator of the request, and typically file under seal documents over which the privilege is being asserted for in camera court review. Outside counsel should be attuned to the bank examination privilege to minimise the risk of unnecessary disclosure, particularly in the current environment where banks are investigated and sued in myriad forums, by a multitude of agencies and private litigants.

ii Attorney–client privilege

Privilege over documents prepared during internal investigations

In the wake of enforcement actions against banks since the financial crisis of 2008, there has been an uptick in internal investigations as banks increasingly play the role of deputised enforcers. Given the concurrent rise in private parallel litigation, there is a greater risk that private litigants will seek discovery of materials prepared in the course of an internal investigation. It is important that a bank's counsel, internal or external, ensure their communications and records concerning the internal investigation remain privileged.

In general, the rule for the attorney–client privilege to apply is that the communication must have been made in confidence for the purpose of obtaining legal advice. US courts have conducted fact-intensive analyses to determine whether the privilege applies. In at least one prominent US jurisdiction, the court has made clear that the correct test was whether 'one of the significant purposes' of the investigation was to obtain or provide legal advice.²¹ Application of that standard to company responses to data breaches, however, has reached

21 *In re Kellogg Brown & Root, Inc.*, 756 F.3d 754, 758-59 (D.C. Cir. 2014).

inconsistent results as to whether a subsequent investigation by a forensic firm produces privileged information.²² In this context, a bank's counsel should ensure that internal investigations are led by attorneys and have adequate attorney oversight.

In addition, given the tendency of regulators, beyond the bank's primary supervisor, to vie with one another to take the lead in investigating potential wrongdoing, care should be taken when disclosing to regulators documents prepared by counsel during an internal investigation. At least one court has recently held that 'oral downloads' of information given by the law firm to the Securities and Exchange Commission are not privileged and therefore must be turned over from the company to former employees of the company.²³ Furthermore, when documents are disclosed to a regulator (e.g., the Department of Justice) that is not the bank's supervisory regulator, the bank examination privilege does not apply and such disclosure would constitute waiver of privilege for private litigation and other regulatory investigations. It is possible that a reduction in duplicative investigations will occur in the future based on a recent announcement by the government that it will seek to reduce the 'piling on' of investigations by multiple agencies; nevertheless, it remains critical to understand the manner in which disclosures to certain agencies may waive privilege.

Cross-border considerations

Maintaining attorney-client privilege becomes an even thornier issue when cross-border considerations enter the picture. Given the global nature of most banks, this issue will increasingly be encountered in banking litigation practice. Foreign courts may refuse to apply US privilege law, subjecting documents created during an internal investigation to disclosure to private litigants.²⁴ Given the global scope of many investigations, banks should be conscious that documents prepared in the course of an investigation could end up being disclosed to foreign authorities and, as a result, be later subject to discovery in civil litigation in the United States on waiver or other grounds.

Moreover, in litigation in the United States, depending on which country's privilege laws apply following a choice of law analysis, there is a possibility that attorney-client privilege may not attach at all.²⁵ Given the limitations on attorney-client privilege in other jurisdictions, counsel should be attuned to the increased risk of exposure to disclosure of documents created during an investigation, both in litigation proceedings in the United States and abroad.

22 Compare *In re Premiera Blue Cross Customer Data Sec. Breach Litig.*, No. 3:15-md-2633-SI, 2017 WL 4857596 (D. Or. 27 October 2017) (finding that documents prepared by forensic firm after data breach were not privileged), with *In re Experian Data Breach Litig.*, No. 8:15-cv-01592, 2017 WL 4325583 (C.D. Cal. 18 May 2017) (finding similar documents were prepared in anticipation of litigation and therefore protected work product).

23 *United States Sec. & Exch. Comm'n v. Herrera*, No. 17-20301-CIV, 2017 WL 6041750, at *1 (S.D. Fla. 5 December 2017).

24 See, RBS Rights Issue Litigation [2016] EWHC 3161 (Ch).

25 See, e.g., *Wultz v. Bank of China Ltd.*, 979 F. Supp. 2d 479 (S.D.N.Y.), on reconsideration in part, No. 11 Civ. 1266(SAS), 2013 WL 6098484 (S.D.N.Y. 20 November 2013) (applying Chinese privilege law, which essentially leaves materials unprotected, to all communications except those related to U.S. legal matters).

iii Subpoenas

International reach

Traditionally, warrants and subpoenas issued by the US government carry territorial limitations and thus do not extend to information located outside the United States.²⁶ Based on that traditional rule, the Second Circuit quashed a government warrant seeking customer emails held by a US company overseas on servers in Ireland. The government appealed that decision to the Supreme Court, which heard oral argument on the matter in February 2018. Shortly thereafter, however, Congress passed the CLOUD Act, which explicitly declares that a provider of electronic communication service or remote computing service is required to comply with the provisions of the Act, regardless of whether the records are located outside of the United States.²⁷ Given the focus of the law on providers of communication or computing services, it is unclear at the time of writing how the extraterritorial reach of the law may affect banks located abroad, if at all. The Act includes provisions that permit a subpoena to be quashed or modified if it would require the provider to violate foreign law, or is otherwise improper based on the comity analysis laid out in 18 USC Section 2703(h)(3). Those provisions will likely prove critical in protecting records stored abroad from use in litigation, particularly in light of the General Data Protection Regulation that took effect in the European Union at the end of May 2018.

Personal jurisdiction

The recent developments in personal jurisdiction case law post-*Daimler*, discussed in greater detail in Section III, above, have provided banks with another tool to defend against subpoenas. While the Federal Rules of Civil Procedure permit the issuance of a subpoena to third parties anywhere in the United States, settled law has established that a court must have personal jurisdiction over the target of a subpoena in order to enforce the subpoena. Given that *Daimler* restricts the principle of general personal jurisdiction to where an entity is 'at home', *Daimler* accordingly narrows the court's ability to enforce a subpoena because of lack of personal jurisdiction, and limits the ability of litigants to obtain worldwide discovery from banks that merely have US branches with no connection to the underlying action.²⁸

Separate entity rule

In New York, the separate entity rule has also been a defence against subpoenas seeking information for accounts held outside of the United States, though outcomes in the subpoena

26 *Matter of Warrant to Search a Certain E-Mail Account Controlled and Maintained By Microsoft Corp.*, 829 F.3d 197 (2d Cir. 2016).

27 CLOUD Act Section 103(a)(1).

28 *Leibovitch v. Islamic Republic of Iran*, 852 F.3d 687 (7th Cir. 2017).

context have differed from the outcomes in the injunction and attachment context. Recent cases have left open the question of enforcement of information subpoenas on foreign banks with operations in New York²⁹ and the issue therefore remains unresolved.

VI FREQUENT CAUSES OF ACTION

i Sanction violation suits

Recent years have seen a notable uptick in the number of civil suits brought in the wake of international sanctions violations. Thus, a US government finding, or admission by a bank, typically in a guilty plea, deferred prosecution agreement or civil settlement with bank regulators, that a company has violated a prohibition on commerce with Iran, for example, may well lead to private litigation.

Plaintiffs have primarily brought such claims under the Anti-Terrorism Act, but have also pursued those claims pursuant to common law or the Alien Tort Statute.³⁰ Under the Alien Tort Statute, courts imply a private right of action by persons who are not US citizens for torts that violate 'the law of nations or a treaty of the United States'.³¹ The Supreme Court, however, recently ruled that such actions cannot be brought against foreign corporations, including foreign financial institutions.³²

Primary liability

The Anti-Terrorism Act, as amended in 2016 (ATA), provides a civil cause of action for treble damages and attorneys' fees for private US persons injured by a terrorist act.³³ Plaintiffs have used this provision to assert claims against banks for effecting wire transfers that either directly provided funds to terrorist groups or that transferred funds to intermediaries who allegedly eventually provided funding to terrorist groups.³⁴ Considerable litigation related to these claims is ongoing. ATA primary liability claims require three elements: (1) injury to a national of the United States; (2) caused by reason of; (3) an act of international terrorism. An act of international terrorism in turn requires both violation of an underlying criminal statute, which for financial institutions typically involves a claim of knowing or wilfully blind support to a foreign terrorist organisation by transferring funds to it, and conduct by the bank involving violence or danger to human life and apparent intent to influence or

29 See, *Vera v. Republic of Cuba*, 91 F. Supp. 3d 561 (S.D.N.Y. 2015) (holding that neither the separate entity rule nor *Daimler* restrictions applied and therefore ordering a Spanish bank to comply with a subpoena for information from branches outside New York, reasoning that the bank had consented to general personal jurisdiction by registering as a foreign bank branch in New York in compliance with New York's statutory regime), rev'd on other grounds *Vera v. Republic of Cuba*, 867 F.3d 310, 315 (2d Cir. 2017); see also *Nypl.*, 2018 WL 1472506, at *2-4 (refusing to exercise jurisdiction over banks based on the presence of branch offices).

30 See, e.g., *Ofisi v. BNP Paribas, S.A.*, 278 F. Supp. 3d 84, 92-93 (D.D.C. 2017), vacated in part on other grounds 285 F. Supp. 3d 240 (D.D.C. 2018).

31 28 U.S.C.A. Section 1350.

32 *Jesner v. Arab Bank, PLC*, 138 S. Ct. 1386, 1407 (2018).

33 18 U.S.C.A. Section 2333.

34 See, e.g., *Wultz v. Bank of China Ltd.*, 32 F. Supp. 3d 486 (S.D.N.Y. 2014); *Lelchook v. Islamic Republic of Iran*, Civil Action No. 15-13715-PBS, 2016 WL 7381686 (D. Mass. 20 December 2016).

coerce a government or population. In *Linde v. Arab Bank*,³⁵ the Second Circuit held that, in applying these requirements, a financial institution's provision of routine banking services to a foreign terrorist organisation or its members will not create civil liability unless the financial institution also knows that the funds it transfers will be used for terrorist activities.³⁶

Claims brought pursuant to the ATA have also been successfully defended on grounds of lack of causation. Courts have interpreted the ATA to adopt the traditional element of proximate causation, which requires that the services provided by the financial institution were a substantial factor in causing the terrorist act, and that the terrorist act should have been reasonably foreseeable to the financial institution.³⁷ At least one other court, however, has interpreted the causation requirement less stringently, finding the requirement satisfied where a knowing contribution to a terrorist organisation was made, even if specifically designated for a nonviolent wing of the organisation.³⁸ Thus, while causation has been a hurdle in every court, it may be a less difficult one to overcome in certain US jurisdictions.

Secondary liability

Further, as the Second Circuit addressed in its *Linde* decision, the 2016 Amendments to the ATA create secondary liability for aiding and abetting such terrorist acts, which does not require proof that the banking services directly caused the terrorism-related injuries.³⁹ Instead, the causation requirement focuses on the link between the injury and the party whom the financial institution aids, as opposed to the injury caused by the financial institution itself. The other two requirements for secondary liability are that the financial institution was generally aware of its role in the terrorist act at the time the services were provided, and that it knowingly and substantially assisted the act. As more cases arise to which those amendments creating secondary liability are applicable,⁴⁰ the legal landscape for these types of claims will likely become clearer. At the time of writing, it appears likely that the pre-eminent defence to secondary liability will now hinge on whether the bank knew that it was playing a part in the commission of terrorist activities by the person to whom it transferred funds.⁴¹

Additionally, there has been an effort by plaintiffs to pursue common law-based claims, rather than statutory based claims, against banks for aiding and abetting human rights violations by foreign states, by violating US sanctions prohibiting transfers of funds to those states.⁴² Because such claims necessarily implicate the acts of that foreign state, they have

35 *Linde v. Arab Bank, PLC*, 882 F.3d 314, 329-27 (2d Cir. 2018) (explaining that 'providing financial services to a known terrorist organisation may afford material support to the organisation' but that such support does not equate to an 'act of international terrorism'); see also *Weiss v. Nat'l Westminster Bank, PLC*, 278 F. Supp. 3d 636 (E.D.N.Y. 2017).

36 *Linde*, 882 F.3d, 327.

37 See, e.g., *Fields v. Twitter, Inc.*, 881 F.3d 739, 744-46 (9th Cir. 2018); *Rothstein v. UBS AG*, 708 F.3d 82, 97 (2d Cir. 2013).

38 *Boim v. Holy Land Found. for Relief and Dev.*, 549 F.3d 685, 697-99 (7th Cir. 2008).

39 *Id.* at 328-29.

40 The 2016 Amendments implemented by the Justice Against Sponsors of Terrorism Act apply to any civil action pending on or commenced after 28 September 2016 that arises out of an injury caused on or after 11 September 2001.

41 See, e.g., *O'Sullivan v. Deutsche Bank AG*, No. 17-CIV-8709, 2018 WL 1989585, at *6 (S.D.N.Y. 26 April 2018).

42 See, e.g., *Kashev v. BNP Paribas, S.A.*, 16-CV-3228, 2018 WL 1627261, at *2 (S.D.N.Y. 30 March 2018); *Ofisi v. BNP Paribas, S.A.*, 278 F. Supp. 3d, 92-93.

been dismissed by at least one court on the basis of the ‘act of state’ doctrine, which bars a US court from sitting in judgment over the acts of a foreign government.⁴³ At the time of writing, however, that decision is on appeal and it remains to be seen whether the use of common law aiding and abetting claims in other contexts, such as terrorism, might be more successful.

ii Financial product-related suits

Banks have traditionally faced lawsuits related to the complex financial products they offer. Although those related to mortgage-backed securities are on the decline as many of these cases have settled in recent years, the litigation in this sphere has grown as banks create increasingly sophisticated financial products and derivative instruments. Litigation usually involves allegations of various forms of fraud, misrepresentation, breach of contract or breach of fiduciary duty, and in particular raising claims as to the suitability of the financial product. While such litigation often includes sophisticated parties, a proposed class action was recently filed against a large US bank based on a change in terms regarding the purchase of cryptocurrencies online using the bank’s credit cards by consumers.⁴⁴ The complaint alleges that the bank changed its policies without notice to treat such purchases as ‘cash advances’, which include fees and high interest rates, in violation of the Truth in Lending Act.⁴⁵ Similarly, a proposed class action was recently filed against another US bank for its alleged classification of Uber and Lyft payments as recurring payments for purposes of charging overdraft fees in breach of the customers’ contracts with the bank.⁴⁶ At the time of writing, it remains to be seen whether either case will survive dismissal, and, if so, whether they will proceed as class actions.

iii Antitrust violation suits: civil suits brought in the wake of antitrust investigations

The latest financial scandals involving antitrust investigations and regulatory settlements, from alleged London Interbank Offered Rate (LIBOR) fixing to alleged manipulation of the FX market, have spawned a new wave of private litigation by investors alleging antitrust violations against banks. The allegations in these class actions, many of which have been consolidated, centre on collusive or anticompetitive behaviour by rate setters or counterparties to transactions and many base their allegations on conduct described in regulatory settlements.

While a number of these cases have settled, litigation continues against the non-settling banks. The banks secured a recent victory in the dismissal of certain claims arising from transactions executed outside the United States, but claims under the Commodity Exchange Act were allowed to proceed.⁴⁷ Recently, claims by a separate class of plaintiffs brought under the Sherman Act as well as California state antitrust laws have been permitted to proceed.⁴⁸ Furthermore, it remains to be seen whether additional classes of indirect-purchaser plaintiffs

43 *Kashef*, 2018 WL 1627261, at *2-4 (dismissing based on the ‘act of state’ doctrine common law claims against a bank for allegedly aiding and abetting acts of Sudan).

44 *Tucker v. Chase Bank USA N.A.*, 18 CIV 3155 (KPF) (S.D.N.Y.).

45 *Id.* 18 CIV 3155 (Docket Entry 1, 10 April 2018).

46 *Karen Alexander v. Bank of America*, 18 CIV 2814 (WHO) (N.D. Cal.).

47 *In re Foreign Exch. Benchmark Rates Antitrust Litig.*, No. 13 CIV 7789 (LGS), 2016 WL 5108131 (S.D.N.Y. 20 September 2016).

48 *Nypl. v. JPMorgan Chase & Co.*, No. 15 CIV. 9300 (LGS), 2018 WL 1276869, at *4 (S.D.N.Y. 12 March 2018) (denying banks’ motion to dismiss antitrust claims brought by individual plaintiffs who purchased allegedly price-fixed foreign currency from the defendants at the benchmark rates).

alleging collusion in the FX market⁴⁹ and classes of customers alleging that certain banks used ‘last look’, a trading practice using complex algorithms that allegedly cancel or delay the processing of FX orders in order to ensure the bank receives a more favourable transaction,⁵⁰ will be able to proceed as well.

In the LIBOR sphere, federal antitrust claims that had previously been dismissed by a lower court for failure to plead antitrust injury were revived in 2016, following a reversal by the Second Circuit, which held that antitrust law did not require plaintiffs to show an injury causing harm to competition in order to allege a conspiracy among market participants when the conduct alleged constitutes a *per se* antitrust violation, as in the context of rate-setting.⁵¹ In 2017, the Supreme Court denied a petition from the banks requesting it to review the Second Circuit opinion, so the case will proceed, focusing on whether plaintiffs are efficient enforcers of the antitrust laws – a requirement for antitrust standing. Earlier this year, the district court certified only a limited class of over-the-counter purchasers of LIBOR-based instruments, but refused to do the same for other proposed classes, in part owing to concerns of standing.⁵²

In addition, reports of regulatory investigations, prior to any settlements, have spawned private litigation. For example, in the wake of reports of investigations into the potential manipulation of prices in the supranational, sub-sovereign and agency (SSA) bond market, various class actions were filed against several large financial institutions and individual traders alleging manipulation of prices in the SSA bond market in violation of the Sherman Act, 15 USC Section 1.⁵³

Recently, one court permitted allegations of spoofing, which is defined in Dodd-Frank as ‘bidding or offering with the intent to cancel the bid or offer before execution’⁵⁴ (at least when supported by collusive messages among traders) to move forward as an improper restraint of trade in violation of antitrust laws, namely the Sherman Act.⁵⁵ That same court, however, likewise recognised the eventual difficulty in proving damages in such actions given uncertainty regarding the exact impact on foreign exchange rates. Accordingly, at the time of writing, it is uncertain whether the spoofing claims will ultimately succeed.

Since antitrust violations can potentially carry treble damages, the growth of class actions based on collusive behaviour potentially exposes banks to significant liability.

VII LIMITATIONS ON LIABILITY

i Causation

In order to hold a defendant civilly liable, plaintiffs must show that the defendant caused their injuries. This causal connection requirement frequently limits a defendant’s exposure to damages. Recently, however, in the securities fraud context, the Second Circuit has been more

49 *Baker v. Bank of Am. Corp.*, 16 CIV 7512 (LGS) (S.D.N.Y.).

50 See, e.g., *Alpari (US), LLC v. Credit Suisse Group AG*, 17 CIV 5282 (LGS) (S.D.N.Y.).

51 *Gelboim v. Bank of Am. Corp.*, 823 F.3d 759 (2d Cir. 2016), cert. denied, 137 S. Ct. 814 (2017).

52 *In re LIBOR-Based Fin. Instruments Antitrust Litig.*, No. 11 CIV. 5450 (NRB), 2018 WL 1229761 (S.D.N.Y. 28 February 2018).

53 *In re SSA Bonds Antitrust Litig.*, No. 16-cv-03711 (S.D.N.Y.).

54 7 U.S.C. Section 6c(a)(5)(C). *Sullivan v. Barclays PLC*, 13-CV-2811, 2017 WL 685570, at *12-13 (S.D.N.Y. 21 February 2017).

55 *Sullivan*, 2017 WL 685570, at *12-13.

lenient with regard to allegations of causation at the initial motion to dismiss stage, including by not requiring plaintiffs to rule out other causes of loss.⁵⁶ As a result, the plaintiffs must only give ‘some indication’ of a ‘plausible causal link’ between the loss suffered and the alleged fraud.⁵⁷ In the sanctions violation context, however, a greater causal connection between the provision of banking services and the sanction violation, or terrorist act, is necessary for primary liability, as discussed in Section VI.i, above.

ii Arbitration agreements

Arbitration agreements have become increasingly common in consumer contracts, particularly in contracts used by large financial service providers offering credit cards, bank accounts, student loans and other financial products and services. Arbitration agreements allow providers to contract for this choice of dispute resolution, ensuring all claims will be adjudicated through arbitration rather than in the potentially more costly traditional court forum. In particular, the rise of class arbitration waivers can limit liability by shielding providers from onerous class litigation and arbitration, where costs and potential damages are much higher. In recent years, the Supreme Court has upheld the enforceability of provisions in arbitration agreements precluding class claims and in 2018, Congress nullified a CFPB rule prohibiting class action waivers, so we can expect the practice to continue.⁵⁸

iii Settlement

Settlement is the predominant method of resolving litigation in the United States, because of the costs of discovery, the absence of an English-style ‘loser pays’ rule and the uncertainty of civil jury trials. Settlements of class actions after adverse decisions on dispositive motions or class certification issues are often preferred owing to the existence of civil jury trials in the United States, which magnify uncertainty for corporate defendants, especially those that are generically ‘unpopular’, like banks.

Recent notable bank settlements include:

- a The US\$480 million settlement in May 2018 between a US bank and a securities-fraud class action of investors who claimed that the bank’s stock traded at artificially inflated prices as a result of the bank’s creation of false customer accounts, and the US\$142 million settlement in March 2017 between that bank and a class action of consumers alleging damages as a result of the bank’s creation of false accounts, which could ultimately exceed US\$142 million because the bank agreed to ensure that each customer claim was fully compensated.
- b The US\$1 billion settlement in April 2018 between a US bank and the CFPB in coordination with the OCC for matters regarding a compliance risk-management programme and past practices regarding automobile loans and mortgages.
- c The US\$42 million settlement in March 2018 between a US bank and the New York Attorney General for misleading customers by telling them stock trades were managed in-house when, in reality, those trades were handled by outside firms.

56 See, e.g., *Charles Schwab Corp.*, 883 F.3d 68, 93-95; *Loreley Fin. (Jersey) No. 3 Ltd. v. Wells Fargo Sec., LLC*, 797 F.3d 160, 188 (2d Cir. 2015).

57 *Charles Schwab*, 883 F.3d, 93 (quoting *Loreley*, 797 F.3d, 188).

58 See, e.g., *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463 (2015); *Am. Express Co. v. Italian Colors Rest.*, 570 U.S. 228 (2013); *AT&T Mobility LLC v. Concepcion*, 563 U.S. 333 (2011).

- d* The US\$66.6 million settlement in March 2018 between a US bank and a class action of consumers who claimed the bank collected unlawfully high interest rates from consumers whose current accounts were overdrawn by charging usurious fees on those overdrawn accounts.
- e* The US\$22 million settlement in January 2018 between a US bank and a class action of consumers who claimed the bank wrongly charged overdraft fees for Uber and Lyft payments, which should have been exempt from overdraft fees as non-recurring payments under the terms of the consumer contracts.

VIII OUTLOOK AND CONCLUSIONS

The United States continues to experience a period of great political uncertainty, and it is unclear what the implications will be for financial institutions. The Trump administration has already revised the tax code and amended portions of Dodd-Frank, which will lessen the regulatory obligations of banks – potentially significantly. Moreover, the administration has reduced the number of new regulations, and is likely to continue on that path. The practical effects for banking litigation may take some time to manifest themselves.

Similarly, while the new administration has appointed conservative and pro-business judges to the US Supreme Court and lower federal courts, how such appointments will translate into judicial decisions in particular cases remains to be seen. State attorneys general in places such as New York and California have also declared their intention to take up the reins of investigatory activity previously conducted by federal regulators of financial institutions.

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Sonali is a specialist in banking and finance with wide experience in Indian and international bank financing. Sonali has advised on numerous international and domestic financing transactions in India across a range of financing products, including structured finance, leveraged acquisition finance, project and asset finance, debt restructuring, debt capital markets and equity financing. Sonali joined TT&A in 2009, prior to which she was at Linklaters, Singapore.

She has recently been advising bidders on potential acquisitions of distressed companies under CIRP and restructuring of existing debt investments by offshore investors. Other notable transactions include the 40-billion-rupee bond issue for Nirma's acquisition of Lafarge's cement assets in India, financing for Blackstone's acquisition of a majority stake in Mphasis, the first partially guaranteed microfinance loan programme in India established by ADB and IFMR, and a covered bond issuance by Andhra Pradesh Expressway Limited, India's first widely syndicated annuity bond.

ALEXANDRA MASON

Allens

Alexandra is a commercial litigator with extensive experience acting in relation to commercial disputes and regulatory investigations for some of Australia's largest corporate clients. Her clients include financial services firms, including leading retail banks, investment banks and accountancy firms, as well as private equity, construction, mining, retail, travel and technology.

Alexandra has been involved in a wide range of complex litigations in Australian courts, including disputes in relation to benchmark manipulation, cartel conduct, misleading and deceptive conduct, unconscionable conduct, breach of contract, breach of directors' duties, auditor negligence and shareholder class actions. Alexandra also specialises in advising clients in relation to major or complex investigations and disputes involving regulators and has dealt extensively with ASIC, the Australian Taxation Office, the Financial Services Ombudsman and the Australian Banking Association.

EMMA MORALES MATA

Linklaters SLP

Emma is a managing associate in the litigation department in Madrid. Emma has more than 10 years' experience advising corporates and financial institutions on a wide range of litigation and arbitration matters. Emma has broad experience in national and international arbitration (ICSID, ICC, CAM, CIMA, CEA) and also in the field of competition law (unfair competition and advertising) and company law (directors' liability, indemnities, breach of contracts).

She has been involved in court trials, appeals and extraordinary appeals for breach of process before the Spanish Supreme Court.

D ROSS MCGOWAN

Borden Ladner Gervais LLP (BLG)

Ross McGowan is national chair of BLG's fraud law group. Ross carries out a broad range of compliance, risk management and litigation support for financial institutions, and industry, with a focus primarily on providing legal advice to financial institutions to combat loss arising from fraud and corruption. He provides advice to financial institutions and others relating to operations, payment systems, policy advice and regulatory compliance. He has acted on matters ranging from litigation defence work of individual customer disputes to mass tort Ponzi scheme claims, and provides operations and compliance advice relating to the design of banking systems, account agreements, policy manuals, anti-corruption regulatory compliance and investigations affecting organisations globally. Ross also works with many insurers, including fidelity, professional errors and omissions, and directors and officers, to provide coverage and subrogation advice relating to fraud losses, bondability of employees, policy design and defence of claims. Ross is also a leading lawyer in the area of commercial leasing disputes, advising landlords, property managers and tenants on an array of issues.

RAGHUVVEER PARTHASARATHY

Talwar Thakore and Associates

Raghuveer is a managing associate with a particular focus on the banking and finance sector. Raghuveer regularly advises clients in relation to various banking and finance transactions, including financing of real estate projects, structured and leveraged finance deals and private placement of debt instruments. Raghuveer recently seconded to the restructuring and insolvency team at Linklaters, Hong Kong, where he was involved in advising on debt restructuring. Raghuveer joined TT&A in 2014, prior to which he was at Phoenix Legal, Mumbai for three and a half years.

STEVEN PETTIGROVE

Linklaters

Steven advises financial institutions and corporates on complex commercial disputes and regulatory investigations, and has particular expertise in advising clients on shareholder disputes and corporate crime. His recent experience includes advising a Hong Kong-listed bank in relation to a dispute with an activist investor and a global financial institution on a cross-border regulatory investigation concerning foreign currency markets.

SASHA ROÉFFERO

Pinheiro Neto Advogados

Sasha Roéffero has been an associate in Pinheiro Neto Advogados' litigation department since 2015, practising in the São Paulo office. She advises on civil and consumer litigation. She completed her law studies at the Mackenzie Presbyterian University (2015), located in São Paulo. She is a member of the Brazilian Bar Association, São Paulo chapter.

CHRISTIAN SCHMITT

Linklaters LLP

Christian Schmitt is a partner at Linklaters in Frankfurt. He is highly experienced in complex litigation and regularly represents some of the most prominent members of the financial community from Germany, Europe and further afield across a broad range of disputes, including insolvency litigation, banking and capital markets-related litigation and contentious regulatory matters. He acts for banks and businesses on a wide range of banking and capital markets issues such as prospectus liability claims, mis-selling and mistrading issues, derivatives and swap litigation, and investment advice liability. He represents clients in all courts and tribunals in Germany (except for the German Supreme Court). Christian Schmitt holds a doctorate from the University of Würzburg. In addition to being admitted to the bar in Germany, he also qualified as a solicitor in England and Wales, and is a certified business mediator. Christian Schmitt regularly lectures at the University of Speyer on issues such as banking supervisory law and bank restructuring.

JONATHAN SWIL

Linklaters LLP

Jonathan is a senior managing associate, having worked in the dispute resolution practice of Linklaters LLP since 2010 and before that at a major Australian firm. He has a broad range of experience advising banks and other financial institutions, professional services firms and corporates on contentious issues and high-profile litigation. His practice has included advising on major contentious insolvencies in the banking and financial services sectors, other contentious matters involving complex financial products and major cross-jurisdictional financial fraud. He also has experience advising in contentious regulatory matters.

HIRONOBU TSUKAMOTO

Nagashima Ohno & Tsunematsu NY LLP

Hironobu Tsukamoto is a partner at Nagashima Ohno & Tsunematsu's New York office. He specialises in litigation and arbitration of a broad range of commercial disputes, employment disputes and intellectual property disputes. Mr Tsukamoto counsels and represents both domestic and foreign clients. In 2015, Mr Tsukamoto moved to Nagashima Ohno & Tsunematsu's New York office and has been assisting our international clients from New York ever since.

He graduated with an LLB from Kyoto University in 1998 and with an LLM from the University of Chicago in 2005. He was admitted to practice law in Japan in 2000, and in New York in 2006.

DANIEL TUNIK

Lenz & Staehelin

Daniel Tunik is a partner in the litigation and arbitration group of Lenz & Staehelin Geneva, and is active in both court litigation and international arbitration. His fields of activity cover all forms of commercial disputes, notably in the banking sector. He is also active in the areas of insolvency law, white-collar crime and employment disputes.

ALESSANDRO VILLANI

Linklaters LLP

Alessandro is a partner and head of the litigation practice of Linklaters in Milan. He has a wealth of experience in a broad range of dispute resolution areas, including banking litigation, bankruptcy and insolvency litigation, corporate litigation, regulatory investigation and arbitration. His client base includes high-profile Italian and international organisations. Alessandro regularly represents clients before the Italian civil and commercial courts and arbitration panels, as well as in European Union court hearings.

Alessandro spoke on usury law in banking contracts and credit protection at a conference organised by the Association of Foreign Banks in Italy in November 2014. He was interviewed about litigation in Italy, together with Loris Bovo and Manuela Caccialanza, by *Getting the Deal Through: Market Intelligence* in November 2016.

Alessandro studied law at the University of Bari. He speaks Italian and English.

Appendix 2

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