Insurance/ Reinsurance

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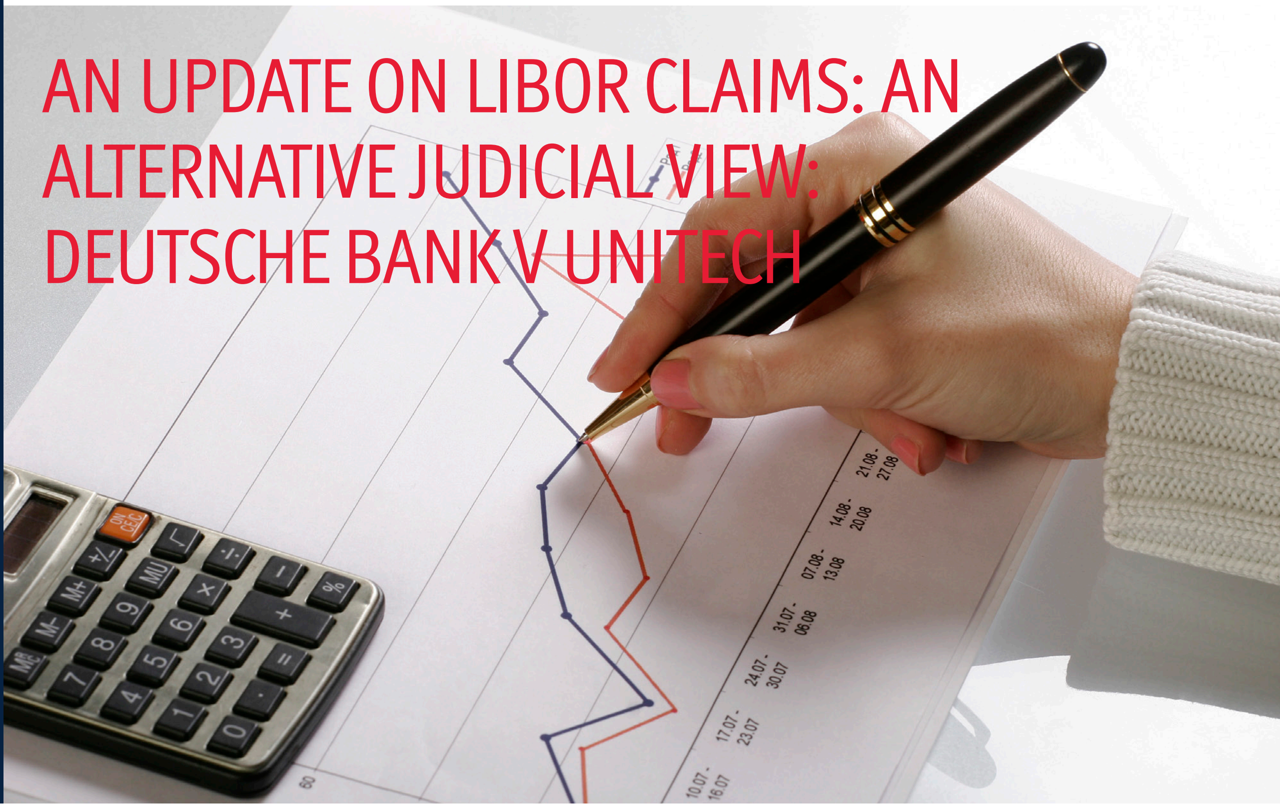
AN UPDATE ON LIBOR CLAIMS: AN ALTERNATIVE JUDICIAL VIEW: DEUTSCHE BANK V UNITECH

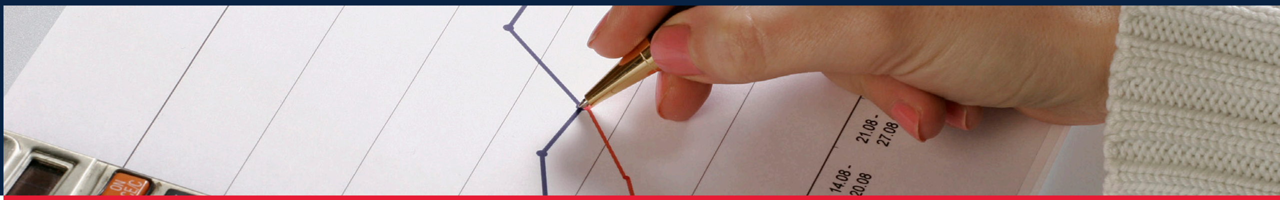


We reported in January 2013, on the continuing developments on LIBOR manipulation and the litigation which has been generated. As readers will be aware interest rate swap (IRS) mis-selling litigation had commenced sometime before LIBOR manipulation came to the fore. However, as a result of the latter, claimants sought to amend their claims to allege LIBOR manipulation in their mis-selling actions.
As previously reported, Mr Justice Flaux in *Graiseley Properties Ltd v Barclays Bank* [2012] EWHC 3093 in proceedings involving IRS mis-selling permitted amendments pleading LIBOR manipulation. However, when the defendants in *Deutsche Bank and Others v Unitech Global and Another* [2013] EWHC 471 sought to plead similar amendments a different outcome resulted.

In *Deutsche Bank* (DB) the defendants sought permission to amend their defence and counterclaims to allege that DB was involved in the manipulation of the Yen LIBOR rate (and potentially others) between 2005 and 2011. By way of background, DB had pursued the defendants for £11 million in respect of an IRS agreement (the swap action) as well as for a further £150 million pursuant to the terms of a credit facility agreement (the lenders' action). The swap agreement was proposed by DB as a hedge against interest rate fluctuations as part of the lending package (which the defendants argued was unsuitable).

The defendants sought to amend their statements of case based on four LIBOR related misrepresentations which they claim induced them to enter into the agreements, and were made negligently, in breach of duty and dishonestly, and that in making the misrepresentations, DB *"gave an implied warranty that the representations were true."*

This implied warranty was said to arise based on DB's membership of the panel of banks that reported daily to the British Banking Association on LIBOR (which informed payments under the IRS agreement). The defendants claimed that DB by its conduct and/or impliedly represented that LIBOR was a genuine average of the rate



at which members of the panel could borrow from one another.

Cooke J however, considered that no such representation was made out simply by DB being a member of the LIBOR panel and entering into a IRS or facility agreement which was linked to LIBOR. One individual bank could not be held responsible for controlling the overall integrity of the system, or other contributions to it, and linking a payment obligation to a LIBOR rate was not enough to give rise to a representation about how that LIBOR rate was, is, or will be compiled. Cooke J noted that:

"What the parties had in mind was the LIBOR rate as it came to be shown on the screen in the future, not what had been done in the past in setting that rate, nor how it would be done in the future, nor what any panel banks' intentions were at the time. Those thoughts would not have crossed their minds as being representations of existing fact being made by DB simply by virtue of contracting by reference to LIBOR and by virtue of DB being a panel bank."

Cooke J also found that the disclaimer of responsibility for any representations contained within the term sheets for the swaps, and a non-reliance representation by the defendants in the swap confirmation made it clear that DB was acting on an arms length basis, and not as their advisor or fiduciary, and it was the defendants' sole responsibility to understand the transaction and make their own independent assessment of its appropriateness. Further, implying any such terms into the contracts would conflict with the entire agreement clauses expressly therein. However, Cooke J said that while the terms of the disclaimer and other contractual provisions were not sufficient to establish a duty of care, the position may be different if in fact dishonesty was established.

Cooke J also noted that the remedy for breach of warranty was based on the assumption that the representations and statements stand as true, for which the proper measure of damages was the difference between any manipulated LIBOR rate and that which would have applied in the absence of such manipulation, and not relief and rescission of the agreement as claimed by the defendants.

This decision is in contrast to that of Flaux J where amendments were allowed to case statements for fraudulent misrepresentation and deceit in relation to LIBOR (albeit this was in relation to Barclays which had, by the time of the amendments, admitted LIBOR manipulation). Perhaps distinguishing this case, Cooke J noted there was no express representation said to have been made by DB to the defendants in the case, which may be in contrast to the evidence presented in *Graiseley* in which it was alleged that representations were made by the various managers and staff in the local branches.

We understand that despite the strongly worded judgment of Cooke J, permission to appeal has been granted in order to reconcile his judgment and that of Flaux J with a view to providing guidance for the widespread LIBOR litigation.

On a connected issue the FSA has published its Internal Audit Report on LIBOR. The Report noted that the FSA was aware of severe dislocation in the LIBOR market between 2007 and 2009, but that this would have occurred without the "low balling". The Report noted various measures going forward to address these LIBOR activities:

- Firms will have to increase their own policing of this activity.
- An effective process for supervisory review of firms' systems and controls needs to be established.
- Escalation of whistle blowing procedures.
- Imposition of exemplary fines (which will no doubt be significant) after the event.

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