

MAYER • BROWN

Hot Topics Affecting the Financial Services Industry

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Hot Topics Affecting the Financial Services Industry

CFTC Investigations and Parallel Private Litigation

CFTC Investigations: Goals and Results

- Recent enforcement actions reflect “CFTC’s unwavering commitment to protect the integrity of critical, global financial benchmarks from profit-driven traders willing to falsify market information We will be relentless in continuing to investigate and bring benchmark manipulation cases until such time as those involved in setting these benchmarks get the message that manipulation will not be tolerated, and the public can be confident in the integrity of these benchmarks.”
 - *Aitan Goelman, CFTC Director of Enforcement*
- CFTC has collected:
 - Over \$906 million in fines between January 2014 – June 2015
 - \$1.7 billion in fines between June 2012 – December 2013

Recent CFTC Investigations: LIBOR

Background

- Short-term interest rate benchmark intended to reflect the cost of borrowing unsecured funds in certain interbank markets
- Used to price a variety of global financial products – futures, swap transactions, home mortgages, commercial and personal consumer loans, etc.
- Panel banks contribute their prices for different tenors - from overnight to 12 months - for different currencies
- Trimmed averaging process

Recent CFTC Investigations: LIBOR

- Parties With Whom CFTC Has Settled: Barclays, Deutsche Bank, ICAP, Lloyds, Rabobank, RBS, RP Martin, UBS
- Alleged Wrongdoing: manipulation of LIBOR and other benchmark rates, in violation of Commodity Exchange Act (CEA)
 - Benefit the bank's trading positions
 - Protect bank from negative market and media perceptions
- Allegedly upon management's instructions or with their consent
- Collusion with traders at other banks and with brokers
- Outcome: Over \$2.6B in settlements
 - Specific steps to ensure integrity of future submissions
 - Continuing cooperation with CFTC

Parallel Civil Litigation: LIBOR

- All of the settling entities – and others – have been sued in private litigation involving substantially similar allegations
- Example: *In Re: Libor-Based Fin. Instruments Antitrust Litig.*, 11-md-2262 (S.D.N.Y. Aug. 12, 2011)
- Alleged Wrongdoing: conspiracy to manipulate USD LIBOR rates, in violation of the CEA, Sherman Act, and state law
- Outcome/Status: Court dismissed plaintiffs' antitrust claims (no antitrust injury); on appeal to Second Circuit
 - MTDs based on failure to state a claim for conspiracy or fraud, and lack of personal jurisdiction, are pending

Parallel Civil Litigation: LIBOR

- Example: *Laydon v. Mizuho Bank, Ltd. et al.*, 1:12-cv-03419 (S.D.N.Y. Apr. 30, 2012)
- Alleged Wrongdoing: conspiracy to fix the LIBOR and Euroyen TIBOR rates, in violation of CEA and Sherman Act, and of state law for unjust enrichment
- Outcome/Status: MTD *granted* as to antitrust and unjust enrichment claims, but *denied* as to CEA price manipulation and aiding and abetting claims

Parallel Civil Litigation: LIBOR

- Example: *Sullivan v. Barclays PLC et al.*, 13-cv-2811 (S.D.N.Y. Apr. 29, 2013)
- Alleged Wrongdoing: conspiracy to fix and manipulation of Euribor, in violation of the CEA, Sherman, and RICO Acts, and of common law for unjust enrichment
- Outcome/Status: Third Amended Complaint filed; U.S. government intervened, discovery was stayed until May 12, 2015

Recent CFTC Investigations: Precious Metals

Background

- Gold Fix - set twice a day, at 10:30am and 3pm, London time
 - Until recently, done by 5 banks that were members of the London Gold Market Fixing Ltd.
- Silver Fix - set daily at noon, London time
 - Until recently, done by 3 banks that were members of the London Silver Market Fixing Ltd.
- Platinum & Palladium fixes - 9:45am and 2pm, London time
 - Until recently, done by four entities that were members of the London Platinum and Palladium Fixing Co. Ltd.
- On dedicated conference line, chairman would open with a price
 - Other banks would relay to customers; price adjusted up or down depending on supply and demand

Recent CFTC Investigations: Precious Metals

- Parties under CFTC investigation: some former members of the London Gold Market Fixing Ltd., London Silver Market Fixing Ltd., London Platinum and Palladium Fixing Co. Ltd., & others
- Alleged Wrongdoing: manipulation of price setting process for gold, silver, platinum and palladium markets
- Outcome: investigations ongoing

Parallel Civil Litigation: Precious Metals

- Many of the entities under regulatory investigation – and others – have been sued in private litigation involving substantially similar allegations
- Example: *In Re: Commodity Exchange Inc., Gold Futures and Options Trading Litig.*, 1:14-md-02548 (S.D.N.Y. Aug. 14, 2014)
- Alleged Wrongdoing: conspiracy to manipulate the price of gold in violation of CEA and Sherman Act
- Outcome: case ongoing; defendants have filed MTDs

Parallel Civil Litigation: Precious Metals

- Example: *In re: London Silver Fixing, Ltd., Antitrust Litigation*, 1:14-md-02573 (S.D.N.Y. Oct. 14, 2014)
- Alleged Wrongdoing: conspiracy to manipulate the price of silver, in violation of CEA, Donnelly Act, and Sherman Act
- Outcome: case ongoing; defendants have filed MTDs

Parallel Civil Litigation: Precious Metals

- Example: *In re Platinum and Palladium Antitrust Litigation*, No. 14-cv-9391 (Nov. 25, 2014 S.D.N.Y.)
- Alleged Wrongdoing: conspiracy to manipulate the price of silver, in violation of CEA and Sherman Act, and for common law unjust enrichment
- Outcome: case ongoing; discovery stayed as of April 21, 2015, until adjudication of defendants' anticipated MTD

Recent CFTC Investigations: Forex

Background

- World Markets/Reuters Closing Spot Rates (“WM/R Rates”), set at 4pm U.K. time - used to establish the relative values of different currencies
- FX benchmark rates, such as the WM/R Rates, are used for pricing of foreign exchange swaps, spot transactions, forwards, options, futures and other financial derivative instruments
- WM/R takes snapshot of trades every second in a window from 30 seconds before until 30 seconds after time of the fix; calculates the median rate to get the benchmark

Recent CFTC Investigations: Forex

- Parties Currently/Formerly Under CFTC Investigation: BofA, Barclays, Citibank, Deutsche Bank, HSBC, JPMorgan, RBS, and UBS
- Alleged Wrongdoing: FX traders coordinated their trading with traders at other banks – including using private chat rooms – to manipulate the FX benchmark rates, in violation of CEA
- Outcome: Orders filed and charges simultaneously settled against most of the banks, for total of nearly \$1.9B
 - Investigation ongoing for Deutsche Bank
 - No CFTC punishment for BofA
- Orders recognize significant cooperation of the banks during CFTC's investigation, including that UBS was the first bank to report misconduct

Parallel Civil Litigation: Forex

- All of the entities under regulatory investigation – and others – have been sued in private litigation involving substantially similar allegations
- Example: *In re Foreign Exchange Benchmark Rates Antitrust Litigation*, 1:13-cv-07789 (S.D.N.Y. Nov. 1, 2013)
- Alleged Wrongdoing: conspiracy to manipulate WM/R Rates, in violation of the Sherman Act
 - Alleged manipulative practices included “trading ahead” or “banging the close”
- Outcome: BofA, Citi, JPM, and UBS settled; other cases ongoing

International CFTC Investigations: Strategic Considerations

Cooperation

- Must decide whether to self report potentially problematic conduct and cooperate in investigation
- Cooperation often entails a thorough internal investigation, proffers of information, production of foreign-located documents, etc.
- But data privacy laws or “blocking” statutes may delay the flow of information

International CFTC Investigations: Strategic Considerations

- Financial institutions have faced enormous penalties – even indictment – where cooperation deemed insufficient
- Must balance desire to move expeditiously with need to comply with foreign laws
- Devise creative strategies to permit compliance with foreign laws while demonstrating cooperation

International CFTC Investigations: Strategic Considerations

Discipline

- U.S. authorities often expect cooperating institutions to discipline culpable employees
- But, can conflict with foreign labor laws, which can limit types of discipline imposed

International CFTC Investigations: Strategic Considerations

Coordination

- Authorities increasingly coordinate with one another and foreign counterparts
- Critical to retain counsel experienced with regulator in each jurisdiction, and for all counsel to communicate regularly

International CFTC Investigations: Strategic Considerations

Discovery

- Broad discovery in U.S. often conflicts with data privacy and blocking statutes in foreign jurisdictions
- Must develop strategies for addressing discovery requests in parallel private litigations

Hot Topics Affecting the Financial Services Industry

UK Perspective on the Interface between Regulatory Proceedings and Court Litigation

Use of Regulatory Investigations as a Tool in Litigation

- Anti-bank litigants may look to interest regulatory authorities in the subject matter of their claim
- Conversely, a regulatory finding may form the basis for a civil action
- Changing climate and attitudes toward banks
- More aggressive claimant/plaintiff activity in the UK and Europe, aided by changing legislation and third-party funding
- What are the implications of concurrent civil proceedings and regulatory investigations?
- How can you best manage those risks?

Use of Regulatory Investigations as a Tool in Litigation II

- Regulatory investigations/litigation may be cross-border
- Parties in the UK and Europe can try to engage U.S. authorities by alleging, e.g.:
 - that relevant activities occurred in the US; or
 - wrong doing involving activities such as corruption of government officials which attract extra-territorial powers
- This brings additional compliance risks (e.g. data privacy)
- Privilege rules may differ across jurisdictions
- Rules on witness evidence (including witness preparation) may differ

Data Privacy and Transfer of Documents to the U.S.

- What happens if a regulator in the US asks to see documents stored in the UK or elsewhere in Europe?
- Data privacy is governed by EU-wide law, enacted in UK as the Data Protection Act 1998 (DPA)
- “Personal data” is very widely interpreted and can extend to information such as an individual’s email address
- “Sensitive personal data”, e.g. political or religious beliefs, health, trade union membership, ethnic origin, sexuality, information about prosecutions / alleged offences
- Breach of DPA may be a criminal offence
- FSA may also fine for breaches

Data Privacy II

- Each stage of discovery/disclosure constitutes “processing” of personal data for the purposes of the DPA/EU Directive
 - Retention (including issuing hold/DND notices)
 - Review
 - Disclosure/inspection
 - Transfer
- The DPA (and equivalent legislation in all EU countries) restricts transfer of personal data outside the jurisdiction to countries the EU considers do not provide an adequate level of protection. This includes the US.

Data Privacy III

- There are derogations, including consent or where the transfer of the data:
 - is necessary for the purpose of, or in connection with, any legal proceedings (including prospective legal proceedings);
 - is necessary for the purpose of obtaining legal advice; or
 - is otherwise necessary for the purposes of establishing, exercising or defending legal rights.
- What does “necessary” mean? Not the same as convenient.
- EU does not necessarily recognise legal obligations imposed by courts/regulators in the US or elsewhere:
 - “An obligation imposed by a foreign legal statute or regulation may not qualify as a legal obligation by virtue of which data processing in the EU would be made legitimate.” (Article 29 Working Party Report)

Data Privacy IV

- Solutions include:
 - Using the procedures of the Hague Convention
 - obtaining a compulsion order from the FCA
 - anonymising materials
 - reviewing materials inside the EU
 - Transfer to a “safe” jurisdiction (e.g. Canada)?
- Even if complying with a court/regulatory order, you still need to remove non-responsive personal data before transfer to US

Sharing Information with Regulators

- Are communications with a UK regulator privileged?
- If you show a regulator privileged legal advice, do you lose privilege?
- As a matter of English law, not necessarily. The FCA Enforcement Guide contemplates accepting material on the basis of a limited waiver of privilege.
- Can a third party obtain the material from the FCA using freedom of information rights?
- Can you share information received from the FCA with third parties? Is it discloseable in litigation?
 - s348 FSMA 2000
 - *Real Estate Opportunities Ltd v Aberdeen Asset Managers Jersey Ltd & Ors* [2007] EWCA Civ 197

Sharing Information with Regulators II

- Can a party share documents it has obtained through disclosure in English litigation with third parties including regulators?
 - Implied undertaking – now CPR r31.22(1)
 - Court gives permission
 - Document is made public through Court process – read by the Court or referred to at a hearing held in public
- Third parties can obtain some documents from the Court file and obtain transcripts of Court hearings.
- In practice, a third party cannot obtain documents from the Trial Bundle from the court once trial has ended (court doesn't retain them).

Is Information Created for Regulatory Investigations Privileged?

- Legal advice privilege (cf attorney/client privilege) – scope is limited
- Litigation privilege (cf work product doctrine) - “litigation” must have been commenced or be reasonably contemplated
- Adversarial rather than inquisitorial in nature
- Investigations and enforcement proceedings that might lead to a punitive sanction
- Investigations aimed at fact-finding or remedial action may not attract litigation privilege
- At what stage does an investigation become “adversarial” in the UK? Less clear cut?

Witness Evidence

- FCA powers to compel evidence – s165 FSMA
- Serious Fraud Office powers – s2 CJA 1987
- Are transcripts of witness evidence discloseable in English litigation?
 - s348 FSMA 2000
- Non-privileged documents obtained for the purpose of litigation?
- Can a witness be compelled to disclose a transcript of his evidence to a regulator? (Third party disclosure order or witness summons (subpoena))
- Can a witness be cross-examined on evidence given in a regulatory investigation?
- What if the regulatory investigation is ongoing?
- Witnesses giving evidence in English courts must not be “coached”

Follow-On Claims in the UK

- Historically difficult in the UK
- But more recently there has been a shift in policy and legislation to enable more “regulation through litigation”
- s90 FSMA 2000
 - Compensation for statements in listing policies/prospectus
- s90A FSMA 2000
 - Liability of issuers for published information

Follow-On Claims in the UK II

- s138D FSMA 2000 (formerly s150)
 - Actions for damages for contravention of a PRA/FCA rule
 - The contravention must have been made by an authorised person
 - Claimant must have suffered loss as a result of the contravention

Follow-On Claims in the UK III

- But only applies to “private persons” (*Titan Steel Wheels Limited v Royal Bank of Scotland PLC* [2010] EWHC 200 (Comm))
- Except:
 - Where there has been a contravention of a rule prohibiting an authorised person from seeking to make provision excluding or restricting any duty or liability.
 - Where there has been a contravention of a rule directed at ensuring that transactions in any security or contractually based investment are not effected with the benefit of unpublished information that, if made public, would be likely to affect the price of that investment.

Follow-On Claims in the UK IV

- FCA can exclude certain breaches from the scope of s138D:
 - Under COBS 4.2.1R(1), a firm must ensure that a communication or a financial promotion is “fair, clear and not misleading”.
 - FCA Handbook states that provided a firm takes reasonable steps to ensure it complies with this requirement, a contravention of that rule does not give rise to a right of action under section 138D of FSMA.

Other Types of Claims

- May be brought related to regulatory breaches, in contract or tort (including fraud)
- Libor claims:
 - *Graiseley Properties Ltd & Ors v Barclays Bank plc and Unitech Limited v Deutsche Bank AG* [2013] EWCA Civ 1372
 - *Guardian Care Homes v Lloyds Bank*
- Claimant law firms in London currently advertising for clients to bring forex claims

Questions?

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