

Biog box

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appropriateness in relation to 'non-complex' financial instruments if certain conditions are met. For these purposes, non-complex products include shares admitted to trading on a regulated market or equivalent third country market (a list of which will be published by the Commission); money market instruments; bonds or other forms of securitised debt (excluding those which embed a derivative); and UCITS. The Level 2 Directive sets out criteria for determining which other types of financial instrument should be considered non-complex. These criteria include the ability to realise the instrument at market price, the availability of comprehensive and understandable information about the instrument's characteristics and the lack of exposure to potential liability exceeding the cost of acquiring the instrument. Derivatives are expressly excluded from the category of 'non-complex financial instrument'.

Reporting requirements: client agreement and client reporting obligations apply in relation to the execution of orders, portfolio management and client assets held by the firm.

Best execution: best execution obligations apply with respect to orders from both retail and professional clients, including the requirement for a firm to have an order execution policy to which clients' prior consent must be obtained – this will be covered in more detail in the next article.

Order handling: rules on the prompt, fair and expeditious handling of client orders and against the misuse of information on pending client orders.

While the substance of the rules is consistent with that of existing requirements in the UK, there is much that is different in the detail. In particular, the extended application of conduct of business rules under MiFID to a

broader range of professional clients will have considerable ramifications for dealings in the inter-professional market, particularly in relation to advice and portfolio management. Firms will need to rewrite their compliance procedures to bring them into line with the new requirements, and also identify opportunities within the new framework.

The revised conduct of business regime will also shape markets. In particular, the appropriateness regime (which is a new concept in the UK), by requiring an assessment of the knowledge and experience of investors prior to undertaking execution-only business with them, will add a layer of complexity to the distribution of structured products which do not fall within the 'non-complex' classification. This will drive providers of retail structured products towards originating non-complex products. ■

BANK AS SECURITY TRUSTEE

Citibank NA v MBIA Assurance SA and another [2006] All ER (D) 196 (Dec) (Chancery Division) (Mann J)

Whether a bank security trustee should accept a direction or exercise its own judgment.

Background

FLF acquired part of the Eurotunnel junior debt in 2000, financed by issuing a series of notes. Certain of the notes have the benefit of a guarantee by MBIA. A hedge fund, QVT, holds certain of the notes. The notes are secured by a trust deed and security arrangement of which Citibank is the trustee. Citibank has direct covenants from FLF under a trust deed and a deed of charge over FLF's assets in its favour. The trust deed gives MBIA the right to give directions to Citibank and exercise extensive control over what would otherwise be Citibank's duties and discretions as a trustee. The deed of charge contains a negative pledge under which FLF covenanted to Citibank as trustee that it will not create security or dispose of its assets without the prior written consent of Citibank and MBIA.

Various Eurotunnel companies, including those liable for that part of the debt acquired by FLF, went into French insolvency 'safeguard proceedings'. A 'safeguard plan' has been proposed, including the replacement of existing debt by new notes redeemable in shares. The intention was that MBIA would cause FLF to dispose of these new notes. QVT objected to this course of action.

MBIA intended to direct Citibank to vote in favour of the 'safeguard

plan'. Due to QVT's attitude, Citibank became concerned whether it could safely accept the direction of MBIA. Citibank as trustee therefore commenced the court proceedings to seek directions.

Conclusions

FLF's rights 'in respect of' the financing agreements assigned to Citibank pursuant to the deed of charge are to be exercised in accordance with the prior instructions of MBIA. The words 'in respect of' are wider than 'under'. They are therefore wide enough to catch a right for MBIA to authorise the substitution of the debt in accordance with the terms of the 'safeguard plan'.

While MBIA has its current role it is given a very large degree of control over the subject matter of the trust. However, the trust regime as a regime remains intact. The trust property is still held on identifiable trusts; Citibank still has functions as trustee; if MBIA does not give directions when entitled to, or when MBIA ceases to hold its position, Citibank will have even more functions. Various powers have been surrendered to MBIA as a matter of commerce. The noteholders all took their commercial interests knowing that MBIA wields the power it wields. The arrangements are not harmful to the trust structure. MBIA has the power to direct Citibank to exercise options under the 'safeguard plan'. ■

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