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CDO Misselling: In *Cassa di Risparmio della Repubblicca di San Marino SpA* ("CRSM") *v. Barclays Bank Ltd* ("Barclays"), Case No: 08-757, High Court of Justice, Queen's Bench Division, the court provided a clear summary of the legal principles that apply in CDO misselling claims, particularly if contractual disclaimer is at issue. Barclays sold CRSM four sets of AAA-rated, credit-linked notes (the "Notes") in 2004/early 2005 having a total face value of €406 million. The Notes matured in 5 to 7 ½ years. In exchange for the principal value of the Notes, CRSM received a coupon for approximately Euribor + 0.95 %. CRSM's central claim was that although Barclays had sold it the Notes on the basis of an AAA-rating that Barclays intended it to rely upon, and upon which it did rely, Barclays knew through internal modeling that the Notes had a probability of default equivalent to B-rated instruments. CRSM further alleged that Barclays deliberately structured the Notes to maximize its own profits.

Barclays's expert witness testified that this practice – known as "credit ratings arbitrage" – was widespread in the structured finance sector during the boom. In many U.S. courts, the claimants have argued successfully that banks engaging in such practices acted fraudulently.

Nonetheless, the court agreed with Barclays that, on the facts, this aspect of CRSM's claim "compared the incomparable." Unlike the Notes' credit rating, the court found that Barclays's internal projection of the risks associated with the Notes was not concerned with default risk. Instead, its purpose was to derive a market price for the Notes to mark its books to market, hedge against the risks associated with the Notes, and calculate notional profits.

Barclays also argued that CRSM's claims were defeated by the terms and conditions of the Notes and disclaimers in the deal documentation. However, the court made it clear that although contracting parties may agree that one party has not made any pre-contractual representations, or that any such representations will not be relied upon, very clear language will be necessary if a term is to be construed as having that effect.

The decision will be welcomed by banks as yet another case in which investors' claims concerning complex financial products have been dismissed. That said, claimants will draw comfort from the court's clarification that misrepresentation claims are contractually excluded only if the banks' disclaimers are sufficiently precise. The key implication is that the stronger the evidence, the more difficult it will be for banks to rely on standard, widely worded disclaimers.

Commercial Contracts: Although disagreements concerning the meaning of contract documents are not new, they are becoming more common in complex debt restructuring cases. Under the "modern approach," contractual interpretation requires a court to decide how a "reasonable person," having all the background knowledge available to the parties, would have understood the words when the contract was made. According to Lord Neuberger, contractual interpretation is now an "iterative process" that requires "checking each of the rival meanings against other provisions of the document and investigating [their] commercial consequences." So long as an argument for a particular interpretation can be made in good faith based on background material and commercial purpose, a party is legitimately entitled to raise that argument. The court will then be required to decide between the alternatives, even if the literal meaning of the contract is clear and unambiguous on its face.

Quinn Emanuel was recently involved in a case (*European Directories* (2010)) which shows how this approach is applied to distressed investments. In *European Directories*, the European Directories group borrowed money under a €1.5 billion senior facilities agreement in exchange for guarantees and security from various group companies. A restructuring was proposed pursuant to which the group's holding company, DH7, would be placed into administration and DH7's shares in its subsidiaries would be sold to a new company. To complete the restructuring, the administrators needed to transfer the subsidiaries' liabilities. They also needed to release the

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guarantees and security granted by DH7 and its subsidiaries pursuant to using a "release on disposals" clause. Under a narrow construction, that clause permitted the administrators to release only DH7's liabilities, not those of the subsidiaries. According to the High Court, the clause extended only to DH7; its purpose had to be determined from its wording, and its scope "should not be enlarged beyond the ambit of the clause itself" so as to apply to the subsidiaries by reference to a priori notions of commerciality. However, the Court of Appeal disagreed, holding that the clause had to be construed broadly and that the administrators' powers extended to the subsidiaries as well. The Court of Appeals reasoned that because the commercial purpose of the clause was to maximize the value of the disposal, in circumstances where a clause was capable of two meanings and neither flouted business common sense, courts should adopt the more commercial construction.

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