The role of the facility agent: reassurance and reminders from the Torre case

“...the question whether [the bank] in fact breached any of its obligations as Agent under the [Facility Agreement] or the Inter-Creditor Deed depends upon analysis of the terms of those agreements. As set out below, I have come to the conclusion that it did not. It matters not that this may be said to have been more by luck than by judgment.”

(Torre Asset Funding Limited & anr v The Royal Bank of Scotland plc [2013] EWHC 2670 (Ch), Mr Justice Sales at 57.)

A. Introduction

The Torre case has been much written about. The legal commentators and the constituency of banks they write for have welcomed a decision which seems to reassure agent banks that the provisions of a Loan Market Association (LMA)-style loan agreement designed to protect the agent are effective.

On the particular facts, Mr Justice Sales narrowly construed the agent’s contractual duties and refused to imply wider terms which he considered would conflict with what the transaction documents were intended to mean and which would run contrary to the widely held perception of the agent’s role as primarily administrative and mechanical. However, the case should not be read as implying that agents cannot have wider obligations for which they may be held legally culpable. Rather, this intricate, sometimes difficult, judgment invites agents to consider all aspects of their behaviour, procedures and systems with a view to eliminating or at least reducing the risk of being held unintentionally liable.

This briefing considers the Court’s approach in considering the duties of the agent (see Section E), and some key issues for agents, lenders and borrowers (see Section I). It concludes with a checklist of questions that an agent might reasonably ask in order to protect itself when dealing with information relating to a facility (see Section J).

Information alone is benign, but its use or misuse, and the timing of its
communication or a failure to communicate it can have serious consequences.

We seek in particular to illustrate the tension between an agent’s administrative and mechanical tasks and the duties arising in connection with the exercise of its discretions.

B. The key legal findings at a glance
The key legal findings were as follows:

> The inclusion of a LMA-style provision stating that the duties of the agent are solely mechanical and administrative in nature will demand a reading of the transaction documents which minimises the substantive content of the duties of the agent (see Section E).

> The common law does not stipulate a set of obligations which attach to all agency relationships, including that of a syndicate agent (see Section F).

Additional obligations, going beyond the express terms of the transaction documents, will not be implied unless it is necessary to do so. Accordingly, the duties of the agent will generally be those, and only those, set out in the transaction documents (see Section F).

> Notwithstanding this, LMA-style facility provisions do confer certain discretions on the agent (see Section F).

> Where the agent is afforded a discretion, it must exercise it in accordance with the principles set out in the Socimer case (see Section F).

> The protective provisions in LMA-style documentation generally only apply to an agent and will not safeguard a bank acting in a different capacity – on its own account as a principal, for instance (see Section H).

C. Background to the dispute
In the latter part of 2006, RBS (the Bank) provided a highly-leveraged, multi-layered financing to Dunedin Property Industrial Fund (Holdings) Limited (the Borrower) to re-finance a large property portfolio held by the Borrower. Each tier of lending had its own loan facility agreement. Each was written in similar terms in all essentials. An Inter-Creditor Deed (Inter-Creditor Deed) governed the relationship between the lenders at the different tiers in the structure.

Some of the senior debt was sold on by the Bank but it kept various roles within the structure, including those in the mezzanine financing. The mezzanine financing comprised three tiers and the Bank’s capacities included acting as agent (Middle Mezzanine Agent) under the middle mezzanine facility agreement (the Facility Agreement) and as agent (Lower Mezzanine Agent) and lender (Lower Mezzanine Lender) at the more deeply subordinated lower mezzanine level.

The deal was severely affected, along with many others, by deteriorating international market conditions in 2007 and 2008. It proved impossible to restructure the transaction and, in September 2008, the Borrower went into administrative receivership. The realisations were less than half the super-senior exposure, and the mezzanine level lenders recovered nothing. The case was brought against the Bank by the middle mezzanine lenders (the Middle Mezzanine Lenders or the Claimants).
D. The claims
The Claimants argued that the Bank, as Middle Mezzanine Agent, had certain duties to pass information about the Borrower on to them, and that at various points during 2007-8 they had failed to comply with these obligations. The Claimants further argued that, if the Bank had complied, the Claimants would have either sold their participation in the loan or sought some form of restructuring and avoided the loss which they eventually suffered. The Claimants argued their case along three lines, which the judge referred to as the "Event of Default Claim", the "Business Plan Claim" and the "Negligent Mis-statement Claim". Each of these are considered further below, but first we consider how the judge analysed and interpreted the agent’s role.

E. The nature of the agent’s role - "solely mechanical and administrative"?
An issue which was central to the case was the Court’s interpretation of the LMA-style "Duties of the Agent" provision in Clause 26.2(e) of the Facility Agreement. Familiar in content, the clause provided that: "The duties of the Agent under the Finance Documents are solely mechanical and administrative in nature."

Just a post box?
Counsel for the Bank argued that the role of the agent was extremely limited. Indeed, the Bank’s team seemed at times to regard themselves acting merely as a post box for documents exchanged between the Borrower and the lenders.

The Court did not accept this "excessively narrow" interpretation. However, it did give considerable weight to the provision, and, in the absence of other expressly prescriptive language, construed the other agency terms narrowly by reference to it.

The Court accepted that standard commentaries on the syndicated loan markets and the LMA precedents were correct in reflecting that the general understanding in the market was that the role of the agent was "intended generally to be limited to an administrative one” and that, in the current case, the "modest level of fee charged by [the Bank] for its services as Agent supported a limited interpretation of the Agent’s role”. But this was not the full answer, and the provision did not afford a linguistic safe-haven for agents.

The Court noted that the LMA model for Clause 26 included exemption clauses. These indicated that the Agent might have wider, more potentially significant duties imposed on it than acting simply as a postal service.

The Court also noted that the Facility Agreement included a number of provisions which appeared to call for the agent’s judgment in a range of situations affecting the syndicate.

The effect of the solely mechanical and administrative provision
The Court concluded that the "solely mechanical and administrative" provision ought to be read subject to specific wording in the relevant agreements which imposed additional duties or conferred discretions on the agent. Mr Justice Sales said:

"Such a reading of the [Facility Agreement] does not deprive Clause 26.2(e) of meaning or effect: the clause mandates a reading of the finance agreements which minimises so far as is possible, consistently with the express language and practical workability of the agreements and the arrangements to which they are intended to give effect, the substantive content of the duties on the Agent. [Our italics]"
Discretions and duties relating to the exercise of them

Significantly, the Court noted that the agent could be required to exercise its discretion under a number of provisions. This went beyond what might be regarded as administrative. Any discretion would be required to be exercised with due care in good faith and in a manner that would not be arbitrary, capricious, perverse or irrational (the Socimer implied term).

In this context, Mr Justice Sales noted two LMA-style provisions in particular. These related to disclosure of information and the manner in which the agent was required to proceed in the absence of instructions from the majority lenders.

Clause 26.6(e) provided that “the Agent may disclose to any other Party any information it reasonably believes it has received as agent under this Agreement” while Clause 26.7(d) provided that “in the absence of instructions from the Majority Lenders ... the Agent may act (or refrain from taking action) as it considers to be in the best interest of the Lenders”.

Commenting further on this, Mr Justice Sales added: “I would add that the relevant standard of what would qualify as arbitrary, capricious, perverse or irrational will be conditioned by the scheme of the contract in which the relevant contractual discretion arises and the commercial purpose intended to be served by the contract. In the context of the [Facility Agreement] a (if not the) principal role of the Agent is to facilitate the [Middle Mezzanine Lenders] in the exercise of their rights and powers under the [Facility Agreement], and what it would be rational or irrational for the Agent to do has to be judged in the light of that... it is my view that if a situation arose in which the Agent under the [Facility Agreement] was told by the Agent for another lending tier that an Event of Default had occurred, the [Agent] would very likely have an obligation under the Socimer implied term to pass that information on to the [Middle Mezzanine Lenders] so that they could consider what to do... the Agent could not simply sit on such information and do nothing.”

One of the reasons why this decision is so important for agents is in what it did not decide. As Mr Justice Sales noted, the Claimants did not plead a case based on a breach of the provision permitting disclosure or a failure to act in “what [the Agent] considers to be in the best interests of the Lenders”. Had the Claimants done so, a reasonable inference might be that the outcome would have been different. It is therefore clear (or at least for now undecided) that an agent could have quite extensive duties based on breaches of provisions giving the agent a discretion.

It was against this backdrop that the Court went on to determine the three main claims.

F. The event of default claim

The facts

Towards the end of June 2007, the Borrower began discussions with the Lower Mezzanine Lender at the Bank regarding a proposal for the rolling-up of the lower mezzanine loan interest until maturity (the roll-up request). The Lower Mezzanine Lender’s model showed that, without the roll-up, it might be difficult for the Borrower to meet regular interest payments on the middle mezzanine facility and that it would be impossible to make scheduled payments of the lower mezzanine interest.

Once it became clear that the consent of the various lenders under the Inter-Creditor Deed would be required, the Lower Mezzanine Lender sought the consent of the other lenders
in the structure including the Claimants. However, and this is relevant to the negligent mis-statement claim discussed below, they sought consent to the roll-up request on the basis that its purpose was to free up cash for capital expenditure to enhance the letting value of the portfolio, and did not say that it was essential to prevent a breach of financial covenants.

**The claim**
The Facility Agreement included an LMA-style insolvency event of default prescribing an ‘Event of Default’ if the Borrower, "by reason of actual or anticipated financial difficulties, commences negotiations with one or more of its creditors with a view to rescheduling any of its indebtedness". The Claimants argued that the roll-up request not only constituted an Event of Default but also that the Bank was aware of this and that, in its capacity as Middle Mezzanine Agent, it therefore had a duty under one or both of the Facility Agreement and the Inter-Creditor Deed to inform the Claimants as Middle Mezzanine Lender about it. As will be seen below, the Claimants argued that this duty to inform arose on several grounds.

**Was there an event of default?**
The first point was quickly dealt with.

The judge considered that the roll-up request did constitute an Event of Default within the “anticipated financial difficulties” provision. He found that the roll-up request was commenced by reason of anticipated financial difficulties and that the financial difficulties were of a “substantial nature” satisfying the test imposed by Blair J. when considering a similar insolvency event of default provision in Grupo Hoteleró Urvasco SA v Carey Value Added SL (2013).

**Did the bank have a duty to notify the claimants of the event of default?**
For the purpose of considering the Court’s fairly lengthy analysis of this issue, it is necessary to make brief references, albeit in summary form, to the express terms of the relevant agreements, which were based on LMA provisions.

**The Facility Agreement Provisions:**

26.1 **Appointment of Agent**
   - Each Lender appoints the Agent to act as its agent under and in connection with the Finance Documents.

26.2 **Duties of the Agent**
   - If the Agent receives notice from a Party referring to this Agreement, describing a Default and stating that the circumstance described is a Default, it shall promptly notify the Finance Parties.
   - If the Agent is aware of the non-payment of any [sum] … under this Agreement, it shall promptly notify the other Finance Parties.
   - The duties of the Agent under the Finance Documents are solely mechanical and administrative in nature.

**The Inter-Creditor Deed Provisions:**

6.7 **Notification of Default.**
Each Agent shall promptly notify each other Agent on becoming aware of any Default. Any Creditor shall promptly on becoming aware of any Default notify its Agent.
On the basis of the particular facts of the case, a duty to notify did not obviously arise under any of the express terms. Accordingly, the Claimants alleged that the duty arose for other reasons.

**Duties arising under the common law**

The Claimants submitted that the Bank owed general duties at common law as an agent and that these duties had not been excluded by the Facility Agreement. They further argued that these duties included an obligation to provide relevant information to the principal which would cover the background information relating to the roll-up request.

The judge firmly rejected this proposition on a number of grounds:

- The Bank was appointed as agent under the LMA-style "Appointment of Agent" provision (Clause 26.1(a) above) which provided that each lender appointed the Agent "to act as its agent under and in connection with the Finance Documents". There was no appointment of the Bank as an agent on some more general basis, and the duties of the Bank as agent were defined exclusively by the transaction documents.

- Agency was a contract made between principal and agent. Like every other contract, the rights and duties of the principal and agent were dependent upon the terms of the contract between them, whether express or implied. It was not possible to say that all agents owe the same duties to their principals; it is always necessary to have regard to the express or implied terms of the contract.2

- The common law did not stipulate a clearly defined set of obligations which attach to every agency relationship unless excluded by agreement.

- Where parties had entered into detailed commercial agreements, it was not plausible to suppose that they intended that some potential additional set of vague and unspecific duties might apply over and above those specified in the agreements themselves.

- While some obligations of an agent at common law may be characterised as fiduciary, the Facility Agreement expressly stated that the agent was not a fiduciary for the lenders.

Accordingly, the Court held that the Bank as Middle Mezzanine Agent owed no relevant duties to the Claimants beyond what could be found in the Facility Agreement and the Inter-Creditor Deed.

**Implied terms**

The Claimants alternatively argued that a number of obligations should be implied into both the Facility Agreement and the Inter-Creditor Deed imposing an obligation on the Bank as Middle Mezzanine Agent to pass relevant information to the Claimants. As noted above, Clause 6.7 of the Inter-Creditor Deed provided “Each Agent shall promptly notify each other Agent on becoming aware of any Default. Any Creditor shall promptly on becoming aware of any Default notify its Agent ...”

The Claimant’s somewhat tortuous arguments were broadly as follows.

Relying on Clause 6.7, the Claimants argued that the Bank, as Lower Mezzanine Lender, had an obligation to inform itself, as Lower Mezzanine Agent, of the default, and then to notify itself, as Middle Mezzanine Agent. The Claimants then further argued that the

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2 (Kelly v Cooper [1993] AC 205)
Bank as the Middle Mezzanine Agent came under an implied obligation to inform the Claimants of any Event of Default.

The Court rejected all these submissions.

**The Facility Agreement**

Dealing first with the Facility Agreement, and applying the criteria for implying terms, the Court found that there was no scope to imply an obligation on the agent to notify any Event of Default.

Amongst the reasons cited for this were (1) that it was not necessary, (2) the proposed implied term would contradict the express terms of the agreements (3) the proposed implied term would not be capable of being defined with sufficient precision to give reasonable certainty of operation, and (4) the express terms of the Facility Agreement already addressed the issue.

> The Court considered of particular relevance here the LMA-style Clause 26.6(e) (*Rights and discretions of the Agent*) provision providing that "The Agent may disclose to any other Party any information it reasonably believes it has received as agent under this Agreement" and the LMA-style Clause 26.7(d) (*Majority Lenders’ instructions*) provision providing that "In the absence of instructions from the Majority Lenders, (or, if appropriate, the Lenders), the Agent may act (or refrain from taking action) as it considers to be in the best interests of the Lenders". The "natural and obvious inference" was that, on receipt of information, the parties intended that the agent should exercise these discretions in accordance with the Socimer principles, which would allow it to pass on relevant information in exercise of its discretion. The proposed implied term would conflict with the express terms of the Facility Agreement by imposing an absolute obligation to pass on such information rather than a discretion to do so.

> The proposed implied term would also give rise to problems of uncertainty since working out whether an Event of Default had occurred "may involve difficult evaluative judgments, and the indications... are that the [agent] should not have responsibility for making such judgements" (in particular because of the "solely mechanical and administrative in nature" provision at Clause 26.2(e)).

**The Inter-Creditor Deed**

The judge held that, for the express notification obligations in Clause 6.7 to trigger, the relevant "Agent" or "Creditor" would need to be aware both of the "event or circumstance" and that such event or circumstance qualified or would qualify as an Event of Default under Clause 23 of the Facility Agreement. The judge concluded that the Bank was not, as a matter of fact, aware that an Event of Default had occurred at the relevant time. Whether that lack of awareness was reasonable or not, was not the test.

The judge gave a narrow interpretation to the provisions pursuant to which the agent might be treated as being aware of an event of default and come under an obligation to act.

He considered that this interpretation was supported in particular by a consideration of the Clause 26.2(e) "solely mechanical and administrative provision", the general scheme of the contractual arrangements (in line with *Re Sigma Finance*) and business common sense (in line with *Rainy Sky v Koomin Bank*).
The list of Events of Default in Clause 23 of the Facility Agreement included many that called for an evaluative judgment to be made before it could be said whether an Event of Default had occurred. It was not consistent with the "solely mechanical and administrative provision" that the agent might have to make such an evaluative judgment.

A narrow interpretation was further supported by a number of other provisions which indicated that the agent was only expected to act where it was clearly identified that something had occurred which qualified as an Event of Default.

Even if the notification trigger had been met (that is, if the Bank had requisite awareness) the judge held that it would not be possible to imply a term into the Inter-Creditor Deed that the Middle Mezzanine Agent would then have a duty to notify the Claimants as Middle Mezzanine Lenders. Although the onward transmission of such information to the lenders was not covered expressly in the Inter-Creditor Deed, there was no lacuna here; the agent had a discretion under Clauses 26.7(d) and 26.6(e) of the Facility Agreement (as referred to above) to pass on such information.

G. The business plan claim

Under the LMA-style information undertakings in Clause 19 of the Facility Agreement, the Borrower was obliged to supply the Annual Budget "to the Agent in sufficient copies for all the Lenders." On October 2007, the Borrower sent the Bank a final version of its revised business plan (prepared as a result of the restructuring negotiations that had begun that summer) (Business Plan) followed by a revised cashflow (October cashflow).

The Claimants argued that the Bank, acting as Middle Mezzanine Agent, should have sent them the Business Plan and October cashflow as the Borrower’s "Annual Budget" for the purposes of clause 19.1(c) of the Facility Agreement (the LMA-style financial information undertakings).

The judge held that the Borrower had not presented the Business Plan and October cashflow as the “Annual Budget” and so the Bank acting as Middle Mezzanine Agent was under no obligation to pass them on.

Furthermore, having regard to the “solely mechanical and administrative” nature of the Bank’s role, the judge held that there was no implied obligation on the agent:

- to pass on to the lenders any financial information received from the Borrower which came into the categories of information set out in the information undertakings, but rather only the information that was expressly required to be passed on;
- to consider from time to time on its own initiative what additional financial information should be sought from the Borrower regarding its financial condition;
- to chase the Borrower to provide the Annual Budget; or
- to inform the lenders of a failure to provide the Annual Budget.

None of these obligations would be consistent with the agent’s duties as set out in Clause 26 and the specific information provision requirements in Clause 19.
H. The negligent mis-statement claim
The Claimants argued that when, in December 2007 and January 2008, the Bank approached the Claimants for their consent as Middle Mezzanine Lenders to roll up the lower mezzanine interest, it negligently gave a misleading impression that the reason for the roll-up was to free up cash for capital expenditure to enhance the letting value, rather than explaining that the roll-up was essential in order to prevent a breach of financial covenants by mid-2008.

The judge found that when the Bank provided the explanation it assumed responsibility for its accuracy and owed" the Claimants a duty of care in tort to take reasonable care to ensure that the explanation was accurate: Hedley Byrne v Heller & Partners [1964] AC 465". Although there was no suggestion that the Bank deliberately lied in making the statements it did, the judge considered that the Bank had given a materially inaccurate and misleading account of the reason for the roll-up request and breached that duty of care.

The judge also agreed with the Claimants that the Bank had given the explanation in its capacity as Lower Mezzanine Lender and that it therefore did not benefit from the Facility Agreement’s LMA-style exclusion of liability clause which was drafted only in favour of the Bank acting as agent.

The negligent mis-statement claim nonetheless failed by reason of the limits on the duty of care. The Bank’s explanation had been proffered only to persuade the Claimants to give their consent to the roll-up request, and not for the purpose of enabling the Claimants to undertake a wider review of their involvement in the transaction. The Bank therefore assumed an obligation to exercise reasonable care to protect the Claimants from losses resulting from a decision whether to agree to the roll-up request. In the event, the roll-up never happened because it was rejected by other parties and the loss suffered by the Claimants therefore could not be said to result from their decision regarding the roll-up request.

I. Some points arising for agents, lenders and borrowers
Agents
  > Although the courts will seek to construe an agent bank’s duties narrowly to respect a provision that the duties of the agent are solely mechanical and administrative in nature, it is necessary to review the transaction documentation to ascertain the agent’s precise responsibilities, including any express duties to disclose information, and the scope of, and any duties relating to, the exercise of any discretions.

  > If the documentation provides a discretion to pass on information to the lenders, to act in the best interest of the lenders or other discretions, agents will need to consider the duty to exercise those discretions in accordance with the principles set out in Socimer which, in the context of a facility, is likely to mean exercising the discretion in such a manner as will facilitate the lenders in the exercise of their rights and powers under the facility.

  > If agents undertake actions outside what is contemplated by the express terms of the documentation, they may assume a duty of care and incur liability.

  > The exclusion and other protective provisions of a facility agreement generally only apply to the agent (or other administrative parties). A bank with more than one role in the transaction needs to consider in which role it takes specific actions and whether or not its actions, in such capacity, are covered by the protective provisions.
Lenders
> Lenders need to be aware that the agent’s duties are essentially very limited. It is up to each lender to undertake its own credit appraisal, monitor compliance and to chase the borrower (through the agent where appropriate) in the event of late compliance or non-compliance.

Borrowers
> Borrowers need to remember that the agent is not an impartial middleman or the borrower’s advocate to the syndicate. The agent acts for the lenders and may have express or implied duties to disclose information to them that it has received from the borrower, irrespective of whether the borrower intended it to be passed to all the lenders.

J. Questions for an agent
Below are nine basic questions that any financial institution might reasonably ask itself when receiving or discovering information relating to a credit facility in which it is acting as agent.

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<th>Question</th>
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<td>1. What information has been received, and was it given to it in its capacity as agent, as a lender or as another party?</td>
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<td>2. From whom was the information received?</td>
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<td>3. Has the information been provided in an agreed form under the finance documents by reference to particular clauses (the audited financial statements or a project budget, for instance), or voluntarily?</td>
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<td>4. Is there any provision that requires the information to be passed on to any person, and, if so, by what time and in what form?</td>
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<td>5. Does it have any duty (express or implied) to investigate or advise in any sense on the content of the information and then make any decision concerning it, either in accordance with agreed criteria or under a general discretion for the benefit of the lenders or a group of lenders (to be exercised in accordance with the Socimer principles)?</td>
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<td>6. Following receipt of the information, if relevant, can it rely on any provision deeming it not to have awareness of facts even when it has actual knowledge of them?</td>
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<td>7. Should it seek instructions from its principals (the majority lenders or all the lenders, for example)?</td>
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<td>8. Does it have any conflict of interest? Are there any clauses in the finance documents which expressly regulate the conflict?</td>
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<td>9. Is it acting in a capacity and in relation to a matter which affords it the protection of an exclusion of liability clause?</td>
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Should you wish to discuss any of the matters raised in this briefing, please speak with a member of our team below or your regular contact at Watson, Farley & Williams.

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