

**FINANCIAL MARKETS LAW COMMITTEE**

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14 March 2003

**ISSUE 56: EMERGENCY POWERS LEGISLATION**

**Note of a meeting held at Lehman Brothers, 13 March at 5.00 p.m.**

**Present:**

Bill Tudor John, FMLC  
Martin Thomas, FMLC Secretary

Pauline Ashall, Linklaters  
Chris Bates, Clifford Chance  
Peter Beales, LIBA  
Patricia Duncan, FOA  
Mark Evans, Travers Smith Braithwaite  
Tim Herrington, Clifford Chance  
Simon Hills, BBA  
Piers le Marchant, Lehman Brothers  
Richard Metcalfe, ISDA  
Michael Raffan, Freshfields Bruckhaus Deringer  
Richard Tredgett, Allen & Overy

Unable to attend: Richard Slater, Slaughter and May

**Background**

It is important to be sure that there are good arrangements in place to maintain the financial system's resilience during major operational disruption.

The FMLC had been asked by HM Treasury on 25 February to consider their new consultation paper<sup>1</sup> released that day on measures that might be taken in the City in an emergency, "The Financial System and Major Operational Disruption", which seeks views both on strengthening of private sector "market-based" approaches to major disruption and on whether new statutory powers to suspend obligations and to direct "financial infrastructure" entities might be useful in extreme circumstances.

Bill Tudor John, Deputy Chairman of the FMLC, had convened a preliminary discussion of this, for which he invited those attending as above, representing expertise in the range of activities and sectors comprising the wholesale financial markets. The purpose of the discussion was to expose views generally and to consider whether it may be in the interests of the wholesale financial markets for a

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<sup>1</sup> [http://www.hm-treasury.gov.uk/consultations\\_and\\_legislation/major\\_operational\\_disruption/consult\\_operationaldis\\_index.cfm](http://www.hm-treasury.gov.uk/consultations_and_legislation/major_operational_disruption/consult_operationaldis_index.cfm)

view to be formed on the consultation from a vantage point that looks at the City as a whole, in which case the FMLC might be able to assist.

The consultation period runs to 25 April. The views expressed and the issues raised may be summarised as follows.

### **How the wholesale financial markets in London reacted on 11 September 2001**

The goodwill seen in New York was also in evidence in the UK. However, there were instances where no consensus was formed of the extent to which the terrorist attacks triggered force majeure clauses, and the extent to which the events resulted in a ‘non-business day’ as defined in contracts, and in consequence it was not clear whether staff could be allowed to go home, or whether they should stay at work to see transactions through. This was invidious for managers.

### **General reactions to the idea of powers to suspend obligations and to direction infrastructure bodies**

Two recurring strands throughout the discussion were:

- that the wholesale financial markets are too interconnected internationally for the foreign dimension to be ignored. The best approach to maintain resilience in so international a financial marketplace must be formulated internationally. The UK may be islands, but the City is not. There could be instances where a UK market participant performs its obligation to deliver in one country but is barred from receiving here payment against that delivery.
- that the case is not yet made out that legal uncertainties resolved by the proposed powers would outweigh those created by them.

Overriding concerns must be the safety of personnel and the avoidance of legal uncertainty. To rely in all eventualities on goodwill may not be enough, especially if the community of people necessary to generate it are unable to communicate with each other.

Direction of infrastructure body powers could be useful, but views can only be tentative without knowing the range of bodies taken to be part of infrastructure. A great deal of the infrastructure is not in the UK, and that which is cannot be dealt with in isolation. Only those who manage infrastructure bodies properly understand what they are and are not capable of in a crisis; it is hard to see how any direction power could be invoked on the strength of better judgement than that of the managers, a point given extra force by the possibility of sanctions for breach of directions.

Any certainty brought by the powers’ existence might be undermined by uncertainty about what circumstances might trigger their use and, perhaps, by hesitation in market-led solutions in anticipation of the powers being invoked. And the powers once created would result in alterations to existing force majeure drafting. One solution might be a hybrid approach: market drafting that amounts to a force majeure clause triggered not by disruption itself but by a public statement from relevant authorities that there has been a disruption event.

It is not clear what powers relevant authorities believe they already have to cancel business or close markets in the event of crisis nor does the consultation paper give information on this.

### **Standard wholesale financial markets documentation and force majeure clauses**

There is no market-wide force majeure definition. Nor necessarily should there be, since different sectors have different interests. The traditional approach in financial contracts has been not to provide at all for failures to perform, the doctrine of frustration being applicable. But it is not clear whether such disparities as there are across the range of market documents result from clear-eyed differences of interest, or from failure to perfect market-wide co-ordination of approaches.

Any comparative analysis of standard wholesale financial markets documentation must consider also definitions of business days, these being of equal importance.

### **Technical remarks**

Neither the Banking and Financial Dealings Act 1971 nor the common law doctrine of frustration appear from the consultation paper yet to have been analysed in detail.

Issues of private international law must be carefully thought out if it is intended to suspend a foreign law obligation that would otherwise be performable in London, both as regards English law and as regards the main relevant foreign laws.

### **The international dimension – what other countries are doing and how this might connect**

There was a very strong view that the City should not be viewed in isolation from the international markets of which it forms part. The effect of disruption and of measures, contractual or legislative, taken to cater for it must be assessed internationally. The infrastructure of the bond market, for example, is in Benelux; and City equity trading relates to foreign exchanges as much as it does to the LSE.

It is not clear what in fact is or has been done in other countries, nor does the consultation paper give much information on this.

### **Assessment of whether FMLC has useful role to play**

The City does not currently have an overview of how matters would proceed under the law and market documents as they stand (nor, it appears, does HMT). That being so, it may be hard to judge what effect legislation of the type canvassed would have, and therefore in what ways it would improve matters. Some analysis of the current position may be useful, to discover if and where there are gaps in preparedness. A kind of boat drill exercise could be imagined.

There is indeed more to be done in “private sector market-based approaches to major disruption”. It is possible that the FMLC could have a role in facilitating a City-wide perspective.

### **Follow-up**

The matter will be discussed next week by the FMLC. There may be some advantage in convening a further discussion.

**March 2003**