

Client Alert

Enforcing an Oral Loan Trade under English Law

April 15, 2020

Any party active in the global secondary loan market will, at some point, come across questions or concerns involving the formation of a binding contract. These may be questions regarding whether an agreement to trade was made, what terms of the trade had been agreed, or even how the rules of contract formation apply to a telephone call, email or instant message conversation. In this global market the first question is: which country's law governs contract formation? The second question is whether oral trades are enforceable in that jurisdiction.

If all of the contracting parties are in England, then English law will likely govern the question of contract formation. More issues arise if parties are conducting business and arranging a trade from multiple jurisdictions. In general, trades documented on forms published by the Loan Market Association ("LMA") are governed by English law, and parties arranging an LMA trade with a London dealer will likely be subject to the principals of contract law and formation as set forth under English law. Where there is no agreement as to the form of documentation to be used and therefore no agreement as to the law that will govern the question of formation of the contract then it is likely the Rome Regulation on the law applicable to contractual obligations (or Rome I) will apply (i.e., in the absence of the parties choosing the governing law, the applicable law is the law of the place where the party which has to perform the main obligations of the contract is normally resident).

In contrast, loan trades in the U.S. market are generally documented on forms published by The Loan Syndications and Trading Association, Inc. (the "LSTA"), which are governed by New York law. The LSTA was instrumental in lobbying for the passage of a New York law that helped clarify the binding nature of oral contracts in loan trading. English law does not have a specific regulatory scheme detailing the enforceability of oral trades, but English common law gives consistent guidance that oral trades are enforceable if they satisfy some of the same key elements required under English common law.

In both England and the U.S., the formation of a binding and enforceable contract often follows a period of discussion (whether this is an in-depth and extended exchange, or time-pressured communications under volatile market circumstances). During these discussions, trading parties may verbally agree some aspects of the contract during a telephone call, and subsequently vary or agree other terms in contemporaneous written communications. As a result, it can be difficult to establish the exact point at which a binding trade was reached, or the precise terms of that trade. In some cases, a party may even dispute the existence of a binding trade, for reasons that have very little to do with their intentions at the time of the trade. When these situations arise in an English-law-governed trading regime, basic contract law principles can help to provide answers, as well as guidance on best practices to avoid counterparties reneging on an oral contract.

What is Required to Form a Contract?

The key elements for an enforceable contract to exist under English law are: offer, acceptance, consideration, intention to create legal relations, and certainty of terms.

An enforceable contract under English law need not be in any particular form. In fact, a telephone conversation can be sufficient to create a legally binding contract, if the key elements of an enforceable contract are present.

Key Elements of a Contract

- Offer: A promise to enter into a contract on certain terms, which must be specific, complete and made with the intention of being bound.
- Acceptance: A contract can only be formed if the offer is accepted in a final and unqualified manner, therefore an accepting party should ensure to accept the offer clearly and explicitly. To be enforceable, an acceptance must also correspond exactly to the terms of the offer, with no changes. Parties should be mindful not to attempt to accept an offer with the expectation that some terms can or will be removed (or negotiated in) at a later stage.
- Consideration: Consideration in commercial situations is often an easy element to find, for example, consideration can be satisfied by the parties agreeing the purchase price for the traded asset.
- Certainty of Terms: Parties to a contract should ensure that the agreement is certain, complete, and with no absence of any key terms. If an agreement is vague, ambiguous or incomplete, a court may conclude that it cannot be enforced, even if the parties intended to create a legally binding agreement. Agreements to negotiate terms at some future date (sometimes referred to as “agreements to agree”) are not normally enforceable under English law due to their lack of certainty.
- Intention: Whether a binding contract comes into being will depend on the underlying intention of the parties. English case law (including *Bear Stearns Bank Plc v Forum Global Equity Ltd.* which involved the sale by Forum of certain bonds to Bear Stearns) has found that even if the parties were silent as to whether a binding contract was formed there could still be an intention to create legal relations. In the *Bear Stearns* case, the court found that a binding oral contract existed even though the parties had only agreed certain aspects of the trade (i.e., the price for a certain number of bonds) whilst deferring other aspects (i.e., the settlement date) until a later date. Despite the fact that the other settlement terms were not discussed, the court held that this did not mean that the agreement was too uncertain to be enforceable as a binding contract.

Oral Agreements

Even though oral contracts are legally enforceable under English law, evidencing the existence of such a contract, or its agreed terms, can be challenging. Oral agreements can easily be disputed, due to lack of certainty or contradiction by either party. As a result, the agreed terms of an oral agreement should also be documented by a written means as soon as possible. This can be done by way of a trade recap or email correspondence confirming the date and terms of the trade, and eventually signing a trade confirmation which includes the key elements required for contract formation.

LMA Trades

If secondary loan trading parties agree to trade under the LMA trading regime, the agreed trade will automatically incorporate the LMA Standard Terms & Conditions by reference. Unless it is expressly agreed that the trade is still “*subject to contract*” or “*subject to a satisfactory form of Trade Confirmation*”, there should be a binding contract at the time of the oral agreement. The LMA Standard Terms & Conditions provide that a binding contract will come into being upon either an oral or written agreement of the terms on the trade date.

Best Practices

A secondary loan trading party will be best placed to enforce an oral trade if they have a clear and specific record of the material terms of the trade, and when such terms were agreed. The key terms to be agreed on the trade date are:

- Borrower name and facility;
- Trade amount;
- Purchase price;
- Interest treatment;
- Collateral requirement (for participations in unfunded revolvers);
- Structure of transaction and form of purchase documentation (e.g., LMA/LSTA documents, par or distressed, assignment or participation);
- Any additional terms of trade, or specific representations and warranties not included in the standard trade documentation.

Once all key terms are agreed, trading parties should expressly and clearly confirm that they have agreed to such terms, and follow-up with a confirmation in writing, by email or through the use of trade recaps, which evidence that an oral contract has been formed.

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