

# Globalization and the Law Related to Credit and Finance- some Remarks

Lars Gorton

<b>1 Background</b> .....	72
1.1 Some Introductory Remarks .....	72
1.2 Financial Matters and the Law .....	73
<b>2 Some Basic Parameters</b> .....	75
<b>3 Law and International Finance</b> .....	77
<b>4 Credit and Financial Law – Different Elements</b> .....	78
4.1 Different Features – who are Involved and what are they doing? ...	78
4.2 Public Law Elements .....	80
4.2.1 Some general points .....	80
4.2.2 Financial supervisors - their roles and competences .....	81
4.2.3 A survey of some EU legislation within the financial field.	84
4.2.4 Banking regulation and banks in distress .....	85
4.2.5 Deposit guarantee schemes .....	86
4.2.6 Derivatives and hedging .....	86
4.2.7 Money laundering and terrorist financing .....	87
4.2.8 Credit rating agencies .....	87
4.3 Private Law Elements .....	88
4.3.1 Some general points .....	88
4.3.2 Private law questions – some aspects .....	89
4.3.2.1 Some overriding points .....	89
4.3.2.2 Loan agreements and some other contract types	91
4.3.2.3 Some questions related to financial security .....	93
4.3.2.4 Trade finance – usage and contract terms and conditions .....	94
4.3.2.5 Financial advice and professional negligence ....	96
4.3.2.6 Some other financial transaction types and instruments .....	96
<b>5 Final Remarks</b> .....	97

## 1 Background

### 1.1 *Some Introductory Remarks*

Several changes have taken place in business generally and on financial markets in particular since the 1970's. Some seem to suggest that there is a kind of financial degeneration in the sense that there is too little variety between the functions of the various financial institutes and too much of the same approaches with respect to solutions chosen. So in this sense the herd principle seems to apply to customers as well as to financial players and also to supervising bodies.<sup>1</sup> "Globalization" has become gradually more applied to business, but it may be questioned whether there is really such thing as "global law" except perhaps in some narrow areas.<sup>2</sup> This also goes for banking and finance sectors.

A number of factors may be discerned in this development. Banks and other financial institutes have to some extent experienced change in functions and structures (*organizational factor*), some of them have become huge (*obesity factor*), there is a considerably larger variety of different financial instruments and products (*product factor*), larger customer groups have appeared with more money available for investments (*customer factor*), many new technical devices have come into being (*technical factor*), and so have new types of exaggerated compensatory systems (*bonus factor*). All this together with the changed role of the government (the public authority, the regulator) through deregulation and reregulation (*administrative factor*)<sup>3</sup> have meant considerable changes. Add to this the increasing importance of credit rating agencies whose activities have also been questioned. All these factors have singularly or together played important roles in the development, which is the basis for the considerations below.

---

1 This is probably also an effect of the market development with fewer and larger financial institutes operating on the financial markets.

2 For a general account of related matters see e.g. Twining, *Globalisation and legal theory*, London 2000. Globalisation questions were discussed earlier by economists than by lawyers, and taking one's basis in positive law, this is understandable. Globalisation has under all circumstances an impact on the legal development. This development is not exactly the same as that which evolved during the 1970's and 1980's when the discussion circled around multinational companies and transnational business. One of the large accounting and auditing firms presently market their services for "global transactions" and "local law". This catches the legal dilemma, namely that there is no clear established "global law", even if business transactions are often international in character. See also the discussion in Wiklund, *Europeisering och globalisering av svensk rätt*, in Festskrift till Ulf Berniz, Stockholm 2001 p. 221 et seq., where he finds that there was a start of globalization of law when the first transatlantic tele cable came into use.

3 This may also involve the question of the government as shareholder in a bank.

## 1.2 *Financial Matters and the Law*

“International financial law” is not a precise concept; it may not even be absolutely truthful.<sup>4</sup> Below I shall largely disregard from legal questions related to insurance and capital markets and mainly focus on banks and certain other financial institutes.<sup>5</sup> This is also something that should be kept in mind when discussing what may be covered by “international financial law”. Apparently “international financial law” is then not a fully adequate term with respect to the discussion below. It is a broader concept than the law related to credit and finance, but it may be used to illustrate a development which has taken place during the last 30-40 years. Undoubtedly financial services in a very broad sense have become increasingly international or global in character. It may be questioned whether the law around these services could be called international, but I believe that a gradual internationalization has characterized the development.

Even “financial law” may not be very precise as a concept. Which legal areas could be embraced by it? Does credit law form part of it? The law related to insolvency? Capital market law? Banking regulations? The law related to promissory notes and bills of exchange? The law on trade finance?

From a Swedish point of view “financial law” in the above sense has not been regarded as a legal topic taught particularly in the law faculties until rather late. “Finance law” at least at some universities earlier covered mainly tax law aspects and some parts of public law.

Parts of what could be described as financial law in a present teaching and research perspective cover private law as well as public law (administrative law) aspects.<sup>6</sup> The private law part would reasonably be regarded as covering

---

4 “Finance” as well as “international finance” are found as concepts in a large number of book titles, such as among several others Wood, *Law and practice of international finance*, London 2008 and Hudson, *The law of finance*, London 2009.

5 I here also use “financial” in a not very precise sense, and rather deal with banks and other financial institutes more narrowly than with “financial matters” more broadly. The Swedish act on banking and financing, Lag (2004:297) om bank- och finansieringsrörelse, does not fully follow the definition in the EU banking directive but in sec. 1:3 and 1:4 respectively defines banking activities and financing activities. Thus 1:3 sets out: “Med bankrörelse avses rörelse i vilket det ingår

1. betalningsförmedling via generella betalningssystem, och
2. mottagande av medel som efter uppsägning är tillgängliga för fordringsägare inom högst 30 dagar.”

(“In the Act, banking business means a business which includes

1. The processing of payment through general payment systems, and
2. The acceptance of deposits from the public which are available to the depositor within at most thirty days.”) Even more narrowly I below tend to focus on credit law aspects.

6 The difference between public law and private law is maintained in several law systems. Also different court procedures are often used in these two different legal areas. The interconnections between them form a basis for this article, but below I rather refer to administrative law than public law. In Swedish law the concept of “näringsrätt” has to my

the law related to promissory notes, bills of exchange and cheques, suretyship (guarantees?), hypothecation, pledge, insolvency etc., but naturally also such central topic as contract law. The administrative and state law part covers such aspects as financial regulation (in my perspective banking regulation in particular), rules on financial supervision and central banking, money laundering and deposit guarantee schemes and also touch upon crisis management etc. The latter part of financial law has expanded immensely not the least in an EU perspective during the last 20-year period.

The particular part of the law related to competition or to the law of corporations (corporate law in a broad sense) and matters geared at capital market law (such as market abuse, take overs etc.) may also be regarded to form part of financial law (but I have left them outside the below reflections). A particular aspect of competition law concerns state aid.<sup>7</sup>

So, there has been an extensive regulatory development from a previous situation to the present one.<sup>8</sup> So far there is no given, common frame around all these various elements of law related to financial matters. Certain parts of banking law rather seem to have been covered by economists in the studies of economics rather than by lawyers in law studies. This at least seems to have been the case in Swedish (and probably Scandinavian) law. So, largely, financial law was an area where lawyers were not much involved except for those working in banks, regulatory agencies, departments of finance and in law firms specialized in various matters related to financial law.

Private law related to financial matters has been in existence for a long time, but has not been particularly geared at the financial markets and financial actors.<sup>9</sup> Rather early some law firms were specialized in questions related to loan agreements and financial security, to transactions involving mergers and acquisitions etc. With the growing markets and the increasing number of transactions, new instruments and players, there has been a growing interest among lawyers in various matters related to the financial law area.

It is nowadays much more common to find topics such as banking law, financial law, international financial law being taught at law faculties around the world. The development started in the US and UK and was rather early in

---

knowledge no immediate correspondence in English. Neither “industrial law” nor “business law” would be the exact equivalent but both may partly cover, but partly have a different coverage.

- 7 A new academic study on state aid in the financial sector has been published recently, Karlsson, *Statliga stöd till banksektorn*, Lund 2011.
- 8 “Financial law” thereby may be gradually developing towards a legal status corresponding to that of “maritime law”, which is also a legal area, which has evolved over a long period, where *lex mercatoria* has met with national law, international conventions and the development of a large number of standard contracts. Particularly during the last several decades the number of international or regional conventions in the public law area has grown. In maritime law there are thus both private law and administrative law aspects, which interrelate to various degree.
- 9 The subject of “banking law” has existed in a narrow sense covering certain items related to promissory notes, cheques and bills of exchange. Also aspects of financial security, property law and bankruptcy law have been dealt with.

Germany and later in France, where there are also chairs in banking law, international finance law, Bankrecht, Kreditwesenrecht, le droit bancaire etc. In Scandinavia there is a similar development although later, slower and less extensive.

Having said so much about “financial law” it seems obvious that it is even harder to pinpoint what could be referred to as “international financial law” let alone “global financial law”. Under all circumstances financial services and credits often cover two or more jurisdictions, and in this respect there are elements of a global perspective in the financial law area. I shall below try to set out certain parameters which could be used to illustrate a development which may or may not in a longer perspective end up in something that might be characterized as international financial law.

Thus, whereas the major legal systems with respect to general matters of private law developed over several centuries the particular rules which were introduced with respect to the administrative law side of “financial law” are more recent and often carried through quicker for more immediate, political reasons, and the international aspects seem to have developed particularly during the last two or three decades. The latter body of law also for various reasons seems to develop in a rather different way than private law.

In a more narrow European perspective EU legislative bodies have played an increasingly important role in the development of financial law beyond national borders, but this development has also to some extent had an effect outside EU, and furthermore certain legislative measures have been taken in conjunction with various international bodies.

It is also evident that Swedish administrative rules nowadays to a large extent follow from international conventions and EU directives. This is also one factor which needs to be taken into consideration. Private law aspects largely have less of an EU perspective. I have chosen for this article the title *Globalization and the law related to credit and finance*, which is certainly a more narrow legal area than global financial law, but it will serve to illustrate several different aspects in the development.

## 2 Some Basic Parameters

As is well known, law develops in different ways. Legislators, courts of different types, but also users and drafters of different instruments and contracts are all involved in this development but on various levels and with different effects with respect to the result.<sup>10</sup> Legal rules and principles thus evolve in different environments. Legislation as well as case law are basically related to a particular jurisdiction, but not seldom as an effect of international conventions and in some instances also with an eye on the development outside

---

<sup>10</sup> A particular account of legal and economic development has been given by Fukuyama, *The origins of political order*, London 2011, where on p. 245 ff. he deals with the origins of the rule of law. See in particular p. 275.

the own jurisdiction.<sup>11</sup> Usage may evolve in a particular surrounding often extending beyond a particular jurisdiction. The same goes for the *lex mercatoria*, which may be seen as a kind of usage.<sup>12</sup> Soft law usually seems to evolve within a particular jurisdiction although soft law principles may be rather commonly used in several jurisdictions. Various standards may be introduced through legislation or recommendations which are not very precise in nature, but subject to legal development, such as best execution, best practice, sound practice etc. Standard documents intended for use in international business add a further dimension to the development.<sup>13</sup>

The concept of international law has traditionally had a specific legal meaning, and outside such specific legal area it may be hard to pinpoint with any exactitude what could be meant by “international” in different legal contexts, such as contract law, sales law or for that matter financial law, since they have all evolved in a national legal surrounding, but where international aspects have been in different ways gradually grafted in.

“International law” often lacks certain legal fundamentals e.g. that a court when deciding a case will normally have to fall back on a national rule or a legislator may only legislate within its jurisdiction. Contracting parties on the other hand may be able to enter into a contract without specifying the applicable law, in which case a court will have to determine which law will apply<sup>14</sup>, and how the law applicable may be used with respect to a particular dispute. The judgment of a court will also be enforceable only according to particular rules under particular circumstances. Having said this it is also necessary to underline that the situation may be more or less complex in different situations.

Thus private law as well as administrative (public) law is basically regarded as national, although there are within both these legal areas principles which

---

11 EU law is in this connection of a different nature since the member countries have a duty to introduce rules which have been adopted by EU through directives, and regulations are immediately applicable in the member countries. Naturally a state which has ratified a convention but does not implement it is in breach of its duty according to the convention but there is not like in EU a court with legal power to take steps in case a directive is not followed in national legislation.

12 With respect to “lex mercatoria” see i.a. Goode, *A new international Lex mercatoria?* In *Juridisk tidskrift* 1999-2000 p. 253 ff. , and Schmitthoff, *Commercial law in a changing economic climate*, 2.ed. London 1981. See also Nerep, *Lex mercatoria and amiable composition in international arbitration – brief notes*. In *Festskrift till Jan Ramberg*, Stockholm 1996 p. 387 ff.

In this context mention should also be made of the Unidroit Principles of International Commercial Contracts, 2d. ed. 2005 (below PICC) and the Principles of European Contract Law (below PECL), which both in their respective preambles spell out that they may apply where a contract has been made subject to *lex mercatoria*.

13 See i. a. Bernitz, *Standardavtalsrätt*, 7 ed. Stockholm 2008 and Cranston, *The rise and rise of standard form contracts: International commodity sales 1800 – 1970*. Jan Hellner in *memoriam*, Stockholm 2007 p. 11 et seq. See further below in 4.3.2.2.

14 They may also agree to insert into the contract reference to international principles of business law or *lex mercatoria* or similar. In deciding individual cases courts may also take into consideration rules and principles that have developed outside its own jurisdiction, see in Sweden the reasoning in the case NJA 2009 p. 672.

have evolved outside the national framework. For the purpose of this article both private and public law aspects will be taken into consideration, also in an international perspective.<sup>15</sup>

### 3 Law and International Finance

Courts are mostly working with legal material from a particular jurisdiction, and legal education is by tradition primarily focused on national rules.<sup>16</sup> Various parts of law have developed in different ways and are based on different ideas and principles. Some principles and ideas have deep roots in society whereas others are of a more legal technical and more recent character. Different societies may have their economic, legal and philosophical foundation based on rather different ideas. Business practices have developed in various ways, but some features seem to have been adopted rather early and broadly, although there may be historic and geographic differences. The *lex mercatoria* as it developed originally is believed to have been growing gradually in order to create common frameworks with respect to particular parts of trade and in different geographical areas.<sup>17</sup> In many instances law has developed (and develops) through imitation or adoption of rules that have evolved elsewhere (sometimes referred to as legal transplant).

An important part of this general development follows from the creation of several old and new bodies (whether of regulatory or business character) appearing on a global (international) or regional level which have designed new forms of legal instruments. There are thus several elements where international aspects play a role. During the last 10-15 years period the concept of global law also seems to have become increasingly recognized, although globalization seems to have rather originated in business and politics. Even if discussed in these terms it is hard to set out in more precise terms what could be covered by “global law”.<sup>18</sup>

This being said (and repeatedly so) it is obvious that law develops in various environments and in different ways, and traditional legislation on national level is by no means the only way. I shall below revert to some of those international or regional organizations which have had an impact in the development of new legal parameters. Environmental questions, human rights questions, natural

---

15 It must be underlined that the below considerations are of outline character with an object to illustrate a development which is undoubtedly taking place.

16 In several parts of law this is, however, no longer true. This is particularly so where EU law has particular importance, and where various international instruments or even legal principles take precedence.

17 *Lex mercatoria* principles gradually evolved beyond traditional jurisdictions with the aim to meet the needs of merchants, but in the traditional sense *lex mercatoria* seems to have been developed within certain geographical areas and used for particular trades (the *law merchant* seems to be a term developed in English law although not fully corresponding to *lex mercatoria*).

18 Maybe the concept of glocal law (global in character but local in practice) is relatively more pertinent.

resource questions have all contributed to new legal developments, which I am not concerned with here, however.

Considering financial law in particular, several elements influence the legal development. Thus, repeated financial crises have led to new efforts to handle related matters on national, regional and international level. But again, it is very hard to try to set out precisely to what extent there is a legal area which could be called global or international financial law. If delving into various parts of financial law we may be able to trace elements which could be said to be international in character and the combination of which may lead to new legal developments.

There are thus various paths of legal evolution, where official bodies take steps to create new rules, where new customs are emerging, where new contracts are developed etc. I shall below try to pinpoint some of these developments with respect to financial law matters.

## 4 Credit and Financial Law – Different Elements

### 4.1 *Different Features – who are Involved and what are they doing?*

Legal frameworks thus evolve on different levels and in various forms, whether as an interplay between administrative rules and private law, and whether also involving soft law and standard form documents. “Usage” plays an important role, not least in connection with trade finance, and Swedish courts sometimes have to take into consideration whether there may exist a particular usage in connection with an individual dispute.<sup>19</sup>

Legislators and different authorities have contributed to the development of new or changed legal frames both nationally, regionally and internationally, but also representatives of the various financial actors have a role in this development. With respect to private law relations collisions sometimes occur between traditional rules and new contract and/or transaction forms. It is not given once and for all that established rules of contract law, sales law, property law character are adapted to new contractual and transaction devices, and similarly administrative rules which have been introduced may turn out to be inadequate in relation to new circumstances. Legal uncertainty, therefore, may arise in a number of situations in connection with the introduction of new financial products.<sup>20</sup>

---

19 See for illustrative purposes and picked rather haphazardly among several cases for instance NJA 1972 p. 1, NJA 2001 p. 191 and NJA 2002 p. 244.

20 With respect to legal risks see in particular McCormick, *Legal risk in the financial markets*, Oxford 2006 not least on p. 2 et seq. and 95 et seq. He there describes how English courts facing legal problems which have not been decided before, sometimes use a common sense and functional reasoning but in other cases fall back on formalistic reasoning. There are similar examples in Swedish law, where however to a much less degree Swedish courts are involved in international financial questions. In *Finansieringsformers rättsliga reglering*, 5th ed. Lund 2010, Adlercreutz & Pfannenstill discuss and analyze some of those financial devices (such as leasing and factoring) which have developed during the latter part of the 20th century. Not least in relation to property law there have been cases where established

In this development we may thus discern the involvement of new players and the gradual establishment of new financial products also leading to changes in the financial markets. As a consequence a number of financial devices were gradually introduced and recognized (often after adjustments) having been tested against the legal framework.<sup>21</sup>

Beside the fundamental private law rules there is, as mentioned, also a growing substance of administrative law, where the financial actors depending on the economic political situation have come to meet new or changed rules. In order to handle financial crises and in order to take steps of counter measures to prevent or limit risks for new financial crises, legislators have chosen to introduce new special rules intended to reduce systemic risk but also to change the power structure.

Private and public law thus develop in different ways although there are interrelations between them. This also means that different administrative bodies and organizations are involved in different connections. Financial activities which evolve in a global environment are believed to need regulation of global character. This is also where a problem arises since financial activities often take place “globally” but the financial institutes are normally established in a particular jurisdiction and a particular transaction may involve two or several jurisdiction as the case may be. The number of bodies involved in the drafting of such legal rules of different character seems to be increasing and there is also growing demand (by some) for global or at least multicountry supervision.

The various bodies involved comprise entities dealing with immediate legislative measures, with the drafting of standard forms and model forms, or in the establishing of soft law principles etc. Some of them are public law bodies related to the United Nations, such as UNCITRAL<sup>22</sup> or UNIDROIT (mainly dealing with private law matters), others are tied to the World Bank, IMF or the Bank of international settlement (BIS)<sup>23</sup>, the European Union, but

---

principles have collided with new ideas and amended principles have thus developed, *see* i.a. Millqvist, *Sakrättens grunder*, 5th ed. Stockholm 2009 where on various points he refers to such judgments and to legal literature where they have been discussed.

In some instances new legislation has been introduced (often due to EU directives), but in others it has been left with the courts to develop legal standards. In some areas legal problems arising in these connections have been attended to within Unidroit or UNCITRAL and some draft conventions or model rules have thus been drafted and published.

21 For an account of the development with respect to the variety of new financial products *see* i.a. Valdez & Molyneux, *An introduction to global financial markets*, 6th ed. London & New York 2010.

22 United Nations Commission on International Trade law.

23 BIS was originally set up to manage the German war compensation after World War I. *See* about this development e.g. Wood p. 346. To-day it is a club for more than 50 central banks. There are within BIS various groups dealing with payment matters and standards for supervision. The Basle Banking Supervision Committee (being a section of BIS) was set up in 1974 after the failure of the German bank Herstatt. The Basle Group is responsible for the various rules (soft law) related to capital adequacy: Basle I (1988) and Basle II (2005), which have both been turned into EU directives and later Swedish legislation, the latest one “lagen (2006) om kapitaltäckning och stora exponeringar” and following the events after 2007/2008 there is a basis for a Basle III, and following various amendments to the EU

also the Groups of 7, 10 or 20 (G7, G 10 or G20) have had an impact on the call for new rules within the financial law area etc.<sup>24</sup> The legal development arising out of the activities of these organizations or bodies vary since apart from EU, none of them, has an immediate legislative power. Under all circumstances they have, however, contributed to the development of a global financial law, or rather parameters of international law character.

Another entity with a different status (and not a legislator), but still with practical, legal impact in the private law sphere, is the International Chamber of Commerce (ICC) which has been involved in the drafting of UCP 600 (latest version)<sup>25</sup> and URDG 758 (latest version)<sup>26</sup> but is also active in the development of various other new documents. There are also several other trade and branch organizations, which may have an impact on the legal development in this legal area.

## 4.2 *Public Law Elements*

### 4.2.1 **Some general points**

Following several financial crises that seem to occur with various intervals and for different reasons, a number of steps have been taken to prevent their effects (i.e. failures in the financial system). The problems and solutions discussed seem to have revolved around certain catchwords, such as “too big to fail”, “systemic risks”, “moral hazard”, “bank runs” etc., and it has been repeatedly stated by the political establishment that the events that took place last are unacceptable.<sup>27</sup> Generally such failures seem to have occurred because banks and other financial institutes have taken too large and not sufficiently evaluated risks, leading to increased risks of systemic failure nature, then in practice also often involving the tax payers to foot the bill.

Whether steps taken to prevent or mitigate the effects of a new financial crisis will prove to be efficient will always remain to be seen, but the general impression is that there is a kind of merry go round revolving around inefficient rules and lax supervision, new stricter rules and measures later deemed as too harsh and then gradually eased together with more relaxed

---

directives there is a proposal for revised rules on capital adequacy (Proposition 2010/11:110).

24 All these bodies are mainly involved in rules of administrative (public) law character. There are not only calls for more regulation, but the political battle-cry after the financial crisis in 2008 and further seems to have been “better regulation”. There is also an increasingly raised question on how much regulation may cost, but this question presently seems to have limited interest.

25 Uniform Custom and Practices related to letters of credit.

26 Uniform Rules on Demand Guarantees.

27 Particular reference could here be given to Hanqvist, *Den offentligrättsliga reaktionen på finanskrisen (kapitalet)*, Förvaltningsrättslig Tidskrift nr. 2, 2011 p. 281 et seq.

supervision.<sup>28</sup> There may also be a risk that before counter measures have been taken which bite, the lessons from the previous crisis have been forgotten before the next crisis occurs. It is also important to keep in mind that steps taken as a consequence of one crisis may not always be suitable for a new situation arising. It is furthermore necessary to keep in mind that too drastic measures may hamper the efficiency and the creativity of the players in the financial sector. This to my understanding means that it is not an easy task to introduce new rules and then at all times follow up their strict compliance. The purpose of rules and the their application may tend to shift as time goes by.

#### **4.2.2 Financial supervisors - their roles and competences**

For (probably) good reasons there have for a long time been requirements for particular regulation and supervision of the financial markets and the players acting on them. The rationale behind such requirements is the particular risks involved in financial activities.<sup>29</sup> This is true for traditional banks where the mismatch between deposits (short term - any amount deposited may be withdrawn at the call of the customer) and lending (often long term or at least on term basis – where the lender is bound for a period).

In several jurisdictions rules have thus been adopted setting out a legal framework for the activities and conduct of banks and other financial institutes. Such rules aim at creating certain standards for various financial markets both with respect to the players acting on them and the financial instruments developed in order that a financial crisis is avoided. The different rules thus introduced aim at creating sound banking practice and prevent banks from running into financial difficulties (maintaining confidence in the financial markets and players and also to protect depositors). There has been a development towards risk based supervision. Furthermore rules have been introduced which aim to mitigate crisis risks through rules concerning the handling of banks in financial distress.

Such various rules may in some cases have a history which goes back in time and have been introduced in countries where a particular financial crisis has occurred. During the last 30 - 40 years some efforts have been made internationally to meet various risks and problems, and in an EU perspective such rules follow from the EU Treaties and secondary rules having in turn resulted in national legislation in the member countries. Gradually, existing national legislation was replaced by various EU directives in order that harmonization be achieved on EU financial markets. The overriding idea is the

---

28 These are psychological factors, hard to deal with through regulation. We may meet similar behavior in commercial negotiations where covenants in financial agreements may be stricter in certain times than in others.

29 In SOU 1998:160 being the basis for the new Swedish legislation on banks and other financial institutes (lag om Bank- och finansieringsrörelse 2004:297) there was a thorough discussion of various risks in the financial sector, systemic risk, operational risk, credit risk, legal risk etc. The Swedish legislation in chapter 1 sets out definitions i.a. of banking activities and financing activities. Chapter 6 contains general provisions related to activities of credit institutes (such as solidity and liquidity, risk management, sound banking practice etc.) and chapter 13 on supervision (The financial supervisory authority, Finansinspektionen – FI).

stability of the financial systems, and in the one end there are rules and supervision and in the other end we meet rules on crisis management.

Largely these several directives cover the activities of banks and other financial institutes (allowing a bank established and supervised in an EU member state to have activities in another EU country without a particular permit – so-called home country control). They also require capital adequacy basically in line with the different Basle agreements, and they have introduced demands for deposit insurance, etc.

With respect to banks and financial institutes regulatory law in particular has expanded considerably, and the need of prudential supervision both on macro and micro level is generally recognized.<sup>30</sup> In this development both the role of a single supervisory authority and the independence of the central bank may have importance although for different reasons and in different respects.<sup>31</sup> At times and in many countries there is a close cooperation between the ministry of finance, the financial supervisor and the central bank, but presently there seems to be a tendency to separate the area of power between the various functions given to them.<sup>32</sup>

In many jurisdictions the central bank has been entrusted with the common duties of supervision of the stability of the financial system and as lender of last resort<sup>33</sup> as well as the supervision of the financial institutes; in other jurisdictions a particular financial supervisory agency has been set up for the control and supervision of the individual banks and other financial institutes, whereas the supervision of the stability of the financial system at large is left with the central bank.

The wisdom has thus for some time been that the role and function of the supervisory agency should be separate from that of the central bank. Following the collapse of the Bank of Credit and Commerce International (BCCI) there was a split of functions of Bank of England and the Financial Supervisory Authority (FSA) was given the task to handle the supervision of various financial entities.<sup>34</sup>

---

30 For a general survey of this development see e.g. Lastra, *Systemic risk, SIFI's and financial stability*. In *Capital markets law journal*. April 2, 2011 p. 197 et seq. with references.

31 For instance Lastra, *Legal foundations of international monetary liability*, Oxford 2006.

32 This was the case in e.g. Sweden during several decades after 1945 where the entity supervising and regulating banks worked in close cooperation with the Swedish Central Bank (Riksbanken) and with the ministry of finance together forming a powerful trinity guiding and commanding the banks. In this way excessive lending was prevented but also commercial development.

33 See i.a. Sjöberg, *Lender of last resort*, in *Financial crises* p. 55 et seq.

34 The effect of the BCCI collapse (which concerned the question of set off between banks) was twofold, both with respect to new rules on netting between banks and accusations against Bank of England for failure in its duty of supervision. With respect to set-off, one of the cases, *MS Fashion Ltd. v. Bank of Credit and Commerce International SA (No 2)* /1993/ Chancery 425 and confirmed in /1993/ Chancery 439 illustrates this question. Wood p. 222 et seq. gives a survey of aspects on netting. See with respect to the development in EU Directive 96/10/EC of the European Parliament and of the Council of 21 March 1996 amending Directive 89/647/EEC as regards recognition of contractual netting by the

The financial crisis starting in 2007/2008 has made the English legislator reverse the wisdom and decided that Bank of England shall again have the duty of comprehensive regulation and supervision. There is undoubtedly a political reason for this change.

The similar division of power was also an approach adopted in some other jurisdictions such as e.g. Sweden, where the Central Bank (Riksbanken) is the supervisor of monetary policy, whereas FI (Finansinspektionen) supervises and regulates among others banks and financial institutes.<sup>35</sup> The independence of Riksbanken follows from the Swedish constitution and is set out more precisely in the particular legislation on Riksbanken (1988:315). FI is in Sweden the single financial regulator. In English terminology some would say that Riskbanken is concerned with macro supervision and the FI with micro supervision. The Swedish legislation existing in the financial area is to a large extent based on EU directives.

This model was also chosen in the EU where the European Central Bank (ECB) not surprisingly shall be independent from the political establishment. There is on EU level as of yet no single body entrusted with the supervision power of individual banks, but during the last few years some bodies have been established which play a particular role for the development. Mention should be made of European Banking Authority (EBA) established in Frankfurt in 2011 to take over tasks and responsibilities for the stability of the financial system, i.a. strengthening the coordination of supervision. In this connection a role is also played by the European Securities and Markets Authority (ESMA) and the new European Systemic Risk Board (ESRB) which is an independent EU body responsible for the macroprudential oversight of the financial system within EU.<sup>36</sup>

The Swedish Parliament (Riksdagen) is the primary legislator, but following particular legislation the Swedish FI has been granted the right to issue particular rules and regulations related to the financial sector. FI also has the task to grant permits, supervise the various financial entities, issue warnings and take other measures, and it may also revoke permits to act as a bank (or other financial entity as the case may be).<sup>37</sup>

---

competent authorities. In Swedish law there has been a discussion on subordinated conditions and set-off; *see* below p 20 note 60.

35 In Swedish law the FI has been entrusted with the right to issue recommendations and regulations (rekommendationer och föreskrifter) with respect to the different banks and financial institutes, and in Sweden these are many and complex. Christensen (NJM Copenhagen 2008) p. 85 et seq. in *Lovgivningskvalitet og enkeltsagsstyret lovgivning* gave an overview of a discussion on the quality of legislation and Innfjord on p. 205 et seq. in *Almene råd og vejledninger – styring og skon* initiated a discussion on particular rules issued by administrative authorities. In Sweden Warnling-Nerep in several cases has criticized the measures taken by FI. She is now on a committee advising FI in sanction matters.

36 On the macro side the European Stability Mechanism (ESM) has been proposed as a mechanism to combat the European sovereign debt crisis.

37 Lag om bank- och finansieringsrörelse (2004:297) in chapters 13-16. This collection of power within one authority has been criticized for good reason, and hopefully some

### 4.2.3 A survey of some EU legislation within the financial field

Against the above background there is need to account for (although far from complete) some of the rules adopted within EU with regard to the financial sector just in order to give a flavour of the activity. Even if Sweden has its own track record within this field Sweden's joining of EU meant a considerable change, and now a great bulk of the financial legislation in Sweden stems from such EU rules. It is therefore necessary to see their importance for administrative rules which has no correspondence in the private law sphere. Most of these EU rules have, although not in an identical way, been transformed into Swedish law. Such rules go back in time to the 1970's but, particularly during the last decades there has been a considerable legal activity.

The basis is the EU Treaty (after consolidation of the Lisboa Treaty)<sup>38</sup> following which a number of directives have been introduced.

The changing legal framework is thus a consequence of deregulation (on national level) and new regulation (on the EU level) in order to enhance competition and harmonization. During several decades a large number of directives have been introduced at this level and also involving other entities on an international (or rather regional) basis.

Most of these are geared at the regulation of banks, capital adequacy and large exposures, money laundering etc.<sup>39</sup> The first banking directive goes back to 1977 followed in 1989 by the second banking directive, which established a single EU banking license and the so-called home country control, and the present directive from 2006 namely the Parliament's and the Council's directive 2006/48/EC.

In 1988 the Basel I (Basel capital adequacy regulation) was introduced and the same year also saw the Directive on liberalization of capital flows.

The Large exposures directive was introduced in 1992, and the Investment services directive in 1993 followed in 1994 by the Directive on deposit guarantee schemes.

In 1999 there was introduced a legislative framework for the single market in financial services through the FSAP (Financial services action plan).

The year 2000 saw the Consolidated banking directive and the Directive on e-money.

The European Parliament and Council Directive 2001/24/EC on the reorganization and winding-up of credit institutions came in 2001, thereby establishing the recognition throughout the EU of certain reorganization measures/winding up proceedings by the home state of an EU credit institution.

In 2002 the Financial conglomerates directive was passed setting a supervision framework for a group of financial entities engaged in cross-sectoral activities.

---

division of power will some time be the outcome. (It has to be admitted, though, that decisions taken by FI may be appealed to administrative courts.)

38 Particularly art. 49, 56 and 63.

39 See about this development i.a. Valdez & Molyneux, *An introduction to international financial markets*, 6th ed. London 2010 p. 370 ff.

In 2005 the EU savings tax directive was introduced regarding exchange of information on savings income, and in 2007 the Payment services directive.

The MiFID (Markets in financial instruments directive 2007/44/EC) came into effect replacing the 1993 Investments directive.

During 2005-2010 a White paper on financial services policy was drafted, and in 2006-2008 Basel I was updated into Basel II and the Capital Requirements directive.

Following the financial crisis during 2007-2009 further and different measures have been taken to prevent or reduce the effects of the events occurred, and also to balance the consequences of further risks, and during the last few years there have also been discussion on the introduction of new rules on capital adequacy, the handling of banks in distress etc.

Mention should also be made again of the Directive on Contractual netting and payment services Directive.<sup>40</sup>

#### 4.2.4 Banking regulation and banks in distress

Beside lag (2004:297) om bank- och finansieringsrörelse which is an important part of the Swedish legislation in the financial area<sup>41</sup>, a number of other rules have been introduced. Following the introduction of the various rules within EU Swedish law adopted i.a. legislation “2006:1371 om kapitaltäckning och stora exponeringar” (capital adequacy and large exposures) followed up in 2007 on “nya kapitaltäckningsföreskrifter” through “FFFS 2007:1”. FFFS 2010:7 contains new rules on the management of liquidity risks. Traditionally there have been no particular rules on bankruptcy of financial institutes but the general bankruptcy rules apply also within this sector. Generally, one may say that banks which have systemic importance will not be allowed to fail but various methods have been used to protect financial stability by bailing them out in one way or the other.<sup>42</sup>

The rules mentioned in 4.2.2 serve to protect the financial systems, to prevent failures in the payment systems, but as history has shown financial crises appear with varying intervals. Subsequent to this fact there have been various efforts to create systems for the handling of banks in financial difficulties.<sup>43</sup>

---

40 See above in footnote 33.

41 There are 16 chapters in the act, which is based on the EU directives on Financial institutes (which is a minimum directive, thus allowing for individual application in national legislation). Chapter 6 sets out the overriding provisions with respect to the activities of credit institutes, risk handling, transparency, soundness, proportionality etc.

42 Mention could be made of various methods used to handle banks in financial distress. In Sweden efforts were made to create a particular order following the financial crisis in the early 1990's, SOU 2000:66 *Offentlig administration av banker i kris*, which did not, however, lead to any legislation. Within EU there is now a Communication regarding “*An EU Framework for crisis management in the financial sector*”, COM (2010) 579 final. In this connection also the EU rules on state aid from 1998/2006 should be kept in mind.

43 For an account of this development in Europe and in Sweden, see Sjöberg, *Handling systematically important banks in distress – some thoughts from a Swedish perspective*, European Business Organization Law Review 12 p. 227 et seq. He there also gives some

#### 4.2.5 Deposit guarantee schemes

Deposit guarantee schemes, also known as deposit insurance, play an important role as stabilizers in the financial system. They are designed to protect bank depositors from the effects of bank failures, but thereby they also serve as stabilizers for the banking sector. By protecting bank depositors from the risk of bank insolvency (up to a maximum amount) bank customers do not have to make a run on a bank in financial trouble in order to withdraw money from their account.<sup>44</sup> In this sense bank guarantee schemes undoubtedly serve both purposes mentioned, although it is designed for the protection of the individual saver.<sup>45</sup>

EU rules have played an important role with respect to national legislation in this area; there are thus rules with respect to deposit guarantee schemes in Directive 94/19 plus amending directive 2009/14/EC as regards coverage and payments. In Sweden the legislation “lag (1995:1571) om insättningsgaranti” was amended on June 16, 2011.

#### 4.2.6 Derivatives and hedging

Derivative instruments and hedge funds have been some of the targets of politicians being seen as particular culprits in the financial crisis starting in 2007, because they are believed to have increased the risks on the financial markets.<sup>46</sup>

Hedge funds are sometimes referred to as shadow bankers, acting as banks, e.g. lenders, without being regulated or at least regulated moderately. The function of hedging may also be similar to credit insurance in that they cover or share different financial risks. Derivatives very briefly may be designed as futures, options, interest rate swaps and credit derivatives.<sup>47</sup>

During the last few years efforts have been made within EU to create a regulatory system around derivatives and hedge funds, and there have been

---

historic account of the recent Swedish development. Lastra in her article on systemic risk also touches on related questions.

44 This is also a good example of the moral hazard problem. Obviously such deposit guarantee schemes may also increase risk through lower financial costs, and also reduce the depositors' care with respect to their choice of reliable banks.

45 In connection with a seminar in Stockholm 2008 on financial crises the role of bank guarantee schemes was discussed in a Scandinavian perspective, see *Finansiella kriser – betalningssystem och skuldförhållanden* (ed. L. Gorton & G. Millqvist), see Kjølner (Denmark) p. 177 et seq., Dyrhaug (Norway) p. 189 et seq. and Thor (Sweden) p. 195 et seq.

46 See on their role Valdez & Molyneux p. in particular p. 415 et seq. and 239 et seq. and Wood, *Law and practice*, London 2008 p. 425 et seq. Hudson, *The law of finance*, London 2009 on p. 1087 et seq. discusses the use of various financial derivatives also including “hedging” (p. 1091). Cf in Swedish law Johansson, *Optioner och terminsavtal*, Stockholm 1998.

47 See i.a. Wood p. 425.

several consultation papers and communications also leading up to legislative proposals.<sup>48</sup>

#### 4.2.7 Money laundering and terrorist financing

Particular rules have evolved regarding money laundering and terrorist financing. These rules have developed on an international level as well as on EU level<sup>49</sup>, and the present Swedish legislation is found in “lag (2009:62) om åtgärder mot penningtvätt och finansiering av terrorism”.<sup>50</sup> In Sweden money laundering is not a crime per se but is regarded to be a consequence of illegal activities of different types, i.a. organized crime, drugs trafficking and withholding of taxes. Again this is an area where rules have been developed both on EU and international level and also where both hard law and soft law rules have been introduced.

#### 4.2.8 Credit rating agencies

Credit rating agencies (CRAs), such as Standard & Poor, Moody and Fitch have played an increasing role during the last decades.<sup>51</sup> Their roles go back to the financing of railroads in the US during the end of the 19<sup>th</sup> and the beginning of the 20<sup>th</sup> centuries with the increased need of rating the railroad stocks and bonds.

The CRAs through the Basle agreements have been entrusted with growing power to judge and evaluate certain financial instruments, companies and states with a view to evaluate the risk of their failure to repay their loans. Their role is connected with the capital adequacy requirements.

The subprime crisis has led to much criticism against the CRAs for their failure to warn of the risks connected with subprime instruments, and politicians and financial supervisors have also pointed at the conflict of risk arising in relation to their activities. They have also been criticized for not having used sufficient diligence when evaluating the risks of certain state bonds.

---

48 The Commission on Sept. 2010 adopted a regulation on OTC derivatives, central counterparties and trade repositories. The regulation i.a. introduces a reporting obligation for OTC derivatives.

49 The Financial Task Force was set up in 1989 by the G7 countries to deal with money laundering and subsequently terrorist financing. Its task was originally mainly of cooperative nature and a body of whistleblower, *see* Wood, *Law and practice*, p. 347, but its present power is far greater. Hudson on p. 335 et seq. deals in some detail with money laundering questions in a UK perspective.

50 The EU money laundering directive (91/308/EEC) provided a basis for the member states' efforts to prevent criminal money from entering the financial system. Following various events a new and revised directive was introduced, and the present Swedish legislation follows the third EU directive 2005/60/EC of the European Parliament and of the council of October 26 on the protection of the financial system for the purpose of money laundering.

51 *See* i.a. Wood p. 332 et seq. and Aline, *The credit rating agency oligopoly from a regulating perspective*, Zürich 2011, where she in some detail delves into some of the related questions. In Swedish law in particular Hanqvist has discussed related questions in a series of articles in *Förvaltningsrättslig Tidskrift* (FT). In FT 4, 2010 p. 351 et seq. he deals with *Kreditvärderingsinstitutens roll och reglering (II)*.

So far there has not been much legislation introduced with respect to CRAs, but in the US some regulations have been introduced and in the EU more drastic measures are being considered.<sup>52</sup>

### **4.3 Private Law Elements**

#### **4.3.1 Some general points**

As indicated earlier, private law rules related to financial law matters involve several areas of law, such as contract law, the law related to payments, promissory notes, cheques and bills of exchange, as well as financial security (pledge, mortgages, suretyship and guarantees). In some of these areas particular rules have been adopted on a national, and in others on an international level. Such rules have evolved on the basis of legislation, case law, soft law, usages, or standard form documents. Sometimes administrative law rules also set out principles which may have impact on private law relations.<sup>53</sup> I shall below touch upon some of these features.<sup>54</sup>

In view of the length of time during which private law has developed it is not surprising that EU has here played a less prominent role as legislator. In particular fields like consumer law measures have been taken within EU in order that harmonization is reached with respect to competition (and rules serving to protect the consumers). With respect to consumer credits such rules have been adopted in the last version through the directive 2008/48/EEC of the European Parliament and the Council on consumer credit agreements, repealing the previous directive 87/102/EEC. This directive is a so-called full harmonization directive. New Swedish legislation based on the directive was introduced through *Konsumentkreditlagen* (2010:1846). This would

---

52 In the US the Credit Rating reform act was enacted in 2006 with a moderate level of ambition. In the EU two sets of rules were adopted on Dec. 7, 2009: the European Parliament's and the Council's regulation (EC) nr 1060/2009 of September 16, 2009 concerning credit rating agencies, the European Parliament's and the Council's directive 2009/111/EC of September 16, 2009 on the amendments to the directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management.

53 Reference to rules of administrative law character is made occasionally in private law disputes, eg. in some cases where the standard set out in an administrative law statute is referred to in order to determine the standard of diligence to be used in connection with the dispute. This is the situation in e.g. NJA 1993 p. 163 and NJA 1997 p. 324 involving the liability of banks as lenders in relation to private sureties (particularly with respect to information). In these cases the court has referred to the standard of care set out in an administrative statute, and depending on the circumstances may conclude that a breach of such provision in the administrative statute will be regarded as negligence. *See* i.a. Gorton, *Lender liability in Swedish law*. *Journal of international banking regulation*, August 2002 vol. 4 no 1 p. 32 et seq.

54 Even if it is hard to determine precisely the distinction between financial law and capital market law, I here leave out rules related to capital markets in the sense of rules concerning associations and various instruments evolved in that connection. It is necessary to keep in mind that this line has been drawn arbitrarily since the investment in shares by a shareholder is closely related to a loan extended to a company although different rules are involved.

traditionally be regarded as a piece of private law legislation, although also containing administrative law aspects.

Otherwise when referring to rules of private law character in an EU perspective there is limited legislation, but general projects such as PECL and the CFR may be seen as having generally greater impact in the creation of private law principles of a less precise and binding character but which may prove to have some impact in the harmonization of rules of private law character within and maybe also to some extent outside EU. It could also be noticed that private law rules are not seldom in different ways interconnected with public law rules. Occasionally there is a collision between these two spheres but in other instances they may combine.

Two private law areas which may be regarded as having particular importance in relation to financial instruments and financial transactions are property law and bankruptcy law.<sup>55</sup> It is evident from case law as well as legal writing that a subject such as “credit law” involves contract law, property law, the law related to promissory notes and bankruptcy law, and that the parties to a loan agreement will have to draft it so as to consider the impact of them all and also to meet the requirements that follow from each of them.

Apart from efforts to create a European civil code and thereby reach broad overriding solutions there have also been some efforts to coordinate certain financial law legislation of private law character. Some such special rules have thus been introduced in EU, and they may have as effects the collision between rules on the EU level and the traditional rules within the various jurisdictions in EU member states. There may also be a structural problem in that particular rules adopted on EU level do not fit into the various national legal systems. This is the case for instance where property law is concerned, where national law is often based on old principles and ideas. In such cases new rules on EU level (e.g. with respect to financial instruments) may conflict with old established rules and principles in the various EU jurisdictions. Sometimes such EU rules are introduced by administrative rather than by private law rules.<sup>56</sup>

### **4.3.2 Private law questions – some aspects**

#### *4.3.2.1 Some overriding points*

Private law basically evolves within individual jurisdictions, but the development is influenced by several factors, the development in other jurisdictions, international conventions, the development of standard

---

55 Briefly mention could be made to the various studies by Benjamin, in particular her *Interests in securities*. Oxford 2000. The concept of property law varies in that some writers consider it to be related to real estate only whereas others seem to use the concept roughly corresponding to the Swedish concept of “saktätt”.

56 As an example I here can mention from Swedish law the old legislation on surety, which is found in the Commercial Book (HB) chapter 10 (pant och borgen- pledge and suretyship). The rules are very few and there is case law filling up the gaps. During the last decade FI in its Föreskrifter och allmänna råd (Rules and general advice) has introduced certain provisions regarding information to be given by banks to sureties, which also has private law consequences.

documents etc. International bodies such as UNCITRAL and Unidroit play a role in this development through legal instruments which may turn into international conventions or into model laws.<sup>57</sup> The convention method is generally a more formalistic approach, and it is normally a cumbersome procedure to change or amend a convention once in force. In order to achieve harmonization it will also be necessary to consider the application of the rules in other jurisdictions.<sup>58</sup>

As mentioned, legal development may also occur through the use of various types of standard contract documents. This has happened with respect to such different transactions or instruments as e.g. securitization, syndicated loans, and derivatives. In this connection lawyers working practically together with financial business enterprises have designed and drafted standard documents intended to meet the needs of the market.

A number of legal questions may then arise, where courts get involved, to judge various documents, contractual provisions and transactions as well as the functions intended by the parties.<sup>59</sup> Furthermore such legal phenomena as procedural law, bankruptcy law, the law of set off etc. will have an impact.<sup>60</sup>

In England a particular committee was set up to evaluate and determine certain legal problems of private law character which may arise in connection with financial transactions and financial documents. Such difficulties may arise in connection with the design and drafting of documentation concerning new devices and instruments but also to discuss and try to solve problems being a consequence of individual cases.<sup>61</sup> Even if such opinions are not of prejudicing

---

57 So e.g. work with factoring and leasing as well as the “Uncitral’s legislative guide on privately financed infrastructure projects.”

58 So for instance the International Sales Convention (CISG) in its art. 7 (1) states: “In the interpretation of this Convention, regards is to be had to its international character, and to the need to promote uniformity in its application and the observance of good faith in international trade”. Such or similar expressions are nowadays often found in international conventions.

59 So e.g. the case *National Westminster Bank plc. v. Spectrum Plus Ltd.* 2005/ UKHL/ (United Kingdom House of Lords) 41 which also illustrates the importance of the terminology used in the loan documentation.

60 Some of the more striking cases in English law concerns the BCCI bank, and one of the much discussed cases concerned *MS Fashion Ltd v. Bank of Credit and Commercial International SA (No 2)* /1993/ Chancery 439. In Swedish law there has been discussion on subordination provisions and set off in Lindskog in *Svensk Juristtidning* 1992 p. 609 et seq. and 1993 p. 358. See also with respect to subordination terms in *NJA* 1997 p. 382 and *NJA* 2003 p. 128.

61 See i.a. McCormick, *Legal risks in the financial markets*, p. 35 et seq. and 66 et seq. regarding “Guidance Notes “ in certain cases through “Statements of Law” issued since the 1990’s, e.g. one “Guidance Notice” from November 1993 concerning “a consensus of the views of the leading practitioners in the field of insolvency and banking law”. I.a. on p. 2 et seq. and 95 et seq. he discusses “legal risk” and describes how English courts facing legal problems which have not been solved before, have sometimes used common sense reasoning but in other cases have used formalistic reasoning as a point of departure. In his survey McCormick refers to a number of situations where he deems that English courts have been able to create new rules for new situations. See also Goode, *Legal problems of credit and security*, 4th ed. London 2008 i.a. p. 94 et seq.

character, they have great value for lawyers working with new instruments and transactions to evaluate legal risks involved.

#### 4.3.2.2 *Loan agreements and some other contract types*

If loan agreements are used as an illustration of the legal development I have already mentioned that there is in Swedish law no specific legislation with respect to them<sup>62</sup>, but the act on promissory note will here have a role as well as contract law (the contract act and general contractual principles) generally. Loan agreements are normally based on standard agreements<sup>63</sup>, and the individual loan agreement is often connected to a promissory note, where the promissory note often may be seen as the acknowledgement of receipt of the loan amount also setting out a promise to pay a certain amount of money as stated in the note.<sup>64</sup> The significance of the promissory note is that it may be a negotiable instrument which could be transferred from one holder to another. Frequently the bank in the negotiations for a loan agreement requests that a clause be inserted entitling the bank to transfer the loan agreement to another creditor, but at least where a negotiable instrument has also been issued, this should be avoided by the borrower, at least unless both are transferred simultaneously to the same person (and then kept together).<sup>65</sup>

Standard loan agreements are often in use on the national markets as well as on international markets. In particular reference could in this connection be made to syndicated loans having a particular role mirroring the legal development here discussed.<sup>66</sup> Also the interrelation between bonds and syndicated loans merits to be noted, since there are certain common features between them although they are in function and design quite distinct from each other in many respects.<sup>67</sup>

---

62 Although with respect to consumer credits legislation based on the EU consumer credit directive may apply. Furthermore the CFR rules could be observed in this connection setting out certain articles with respect to loan agreements.

63 Earlier the Swedish banking association has been designing and drafting various standard documents used by banks in relation to consumers as well as to commercial borrowers. Today it seems that the particular banks are often drafting their own standard documents, and in international business they are often assisted by foreign lawyers.

64 The Swedish legislation on "skuldebrev" (which bears some resemblance with promissory notes in English law) is a legislation common for the Nordic countries.

65 From the bank's point of view the right to transfer a loan or parts of it is of great importance since this may be a way of the bank to reduce its risk.

66 A syndicated loan is a loan where several banks together grant and extend a credit, *see e.g.* Wood, *International loans, bonds, guarantees, legal opinions*, 2. ed. London 2007 in for example chapter 5 and Mugasha, *The law of multi-bank financing. Syndicated loan and the secondary loan market*, Oxford 2007.

67 *See* Wood, *Law and practice*, chapters 7-12 illustrate these questions, and in particular in *Bondholders and banks – why the difference in protections?* *Capital Markets Law Journal* vol. 6 nr. 2, 2011 p. 188 et seq. Wood compares bonds and syndicated loans from some particular points of view and also questions to some extent the differences in protection of banks as lenders and bondholders as lenders.

Previously syndicated loan agreements were designed and drafted individually by law firms acting for the bank(s), but nowadays the law firm in stead normally uses as a basis the particular loan documentation developed by Loan Market Association, the so-called LMA terms.<sup>68</sup> This documentation allows for the choice for different situations. LMA documents have been drafted mainly to be used for syndicated products of different kinds, but they are mainly used for negotiation purposes, where the negotiating parties may use the documentation as a kind of checklist allowing for amendments in the basic documentation. The LMA terms are thus not “true” standard terms, in the sense that they are intended to be used without amendments (although the individual part of a contract may contain individual clauses which are in conflict with those of the printed form), but they are rather used as a template, a basis for the negotiations between the parties.<sup>69</sup> This template is based on English law being applicable, but the parties may nevertheless agree that the loan agreement be governed by another law system.<sup>70</sup> The LMA-conditions have a fundamental importance with respect to syndicated loans. LMA is quick to adjust the different provisions to meet new requirements, and regularly amendments are suggested in order that new legal challenges may be met. They have also in a relatively short time become widely spread. Even if an individual loan transaction has been made subject to Swedish law, the LMA conditions are often used as a model, but they should then in relevant parts be adapted to Swedish legal conditions and terminology, which is not always easy. As is well known English terminology and legal solutions emanating from English law are not always the same as those developed or not yet available in Swedish law, and particular legal questions may arise when standard conditions designed in accordance with one legal system have been made subject to the law of another jurisdiction.<sup>71</sup>

Another internationally developed contract form is the ISDA documentation, which has its roots in “Anglo-American” law.<sup>72</sup> The ISDA documentation has been developed for various derivative products, and is basically recognized as a standard form agreement which is of more or less take-it-or-leave-it-type.

Another type of international standard conditions are UCP and URDG respectively which will be more discussed below in 4.3.2.4.

---

68 Mugasha gives in chapter 5 (particularly 5-70 et seq.) a description of LMA and the LMA-terms.

69 Since many standard forms are to-day available in electronic form it is not always easy to make the distinction between the standard form and the individually negotiated contract.

70 A similar template has been made in French, *see e.g. Bouretz, Stoufflet & de Vauplane, Crédits syndiqués. Transfert et partage du risque entre banques.* Paris 2005 p. 48 et seq.

71 About this question *see i.a. Gorton, The reception of Anglo-American contract practice into Swedish law: some points on charter parties and syndicated loans*, in Liber amicorum Guido Alpa (ed. By M. Andenaes and several others) London 2007 p. 475 et seq. and Lindholm, *Fremmede retsbegreber i nordisk kontraktsret*, in NJM 2008 p. 611 et seq.

72 *See further below in 4.3.2.5.* It should, however be noted that the notion of “Anglo-Americanlaw” is a misnomer even if there is a basis of common law in the various US law systems.

#### 4.3.2.3 *Some questions related to financial security*

One particular area of private law where Swedish law does not allow for a high degree of contractual arrangements is the law of property (that part of the law which in Swedish is referred to as “sakrätt”, i.e. where two or more parties have claims for the same property, e.g. one is a pledgee and the other claiming to be a buyer, or one is the pledgee and the pledgor is bankrupt). This is a legal domain where there is established legislation in many respects but where case law has sometimes modified the established rules, and where new legislation has proved to be rather cumbersome to achieve. Not least due to various EU directives there have been amendments to the traditional Swedish rules, which do not always fit well into the Swedish system but they serve the purpose of creating more harmonization between the EU countries. This is also a legal area where Swedish courts have to some extent adapted established rules to new conditions.

Furthermore this is a legal domain, where to some extent the implementation of EU directives has led to the introduction of new rules which collide with since long established Swedish rules and particularly with the Swedish legal structure. Thus the Directive on financial collateral arrangements led only to minor adjustments in Swedish legislation,<sup>73</sup> but the directive gives an illustration to the collision between Swedish traditional property law and new EU-rules.<sup>74</sup>

I shall not here delve very much further into related questions, but suffice it to say that from a financial law perspective the differences existing between several jurisdictions as to property law and bankruptcy law may cause problems in the drafting and adapting of documentation related to loan transactions. In particular questions related to financial security need to find a reasonably clear answer, although the particular solution chosen in an individual case may prove not to meet the requirements under a particular law. This is an area where the efforts of finding common solutions often meet insurmountable problems from varying legal ideas and different legal concepts which have evolved in different legal systems.<sup>75</sup> Property law seems to be a legal area where the particular solutions established in different jurisdictions are most difficult to overcome.

We may thus discern a development of various financial instruments and transactions where the contractual elements may be handled in relation to an individual jurisdiction, but where questions of property law character may be responded to in different ways.

---

73 The European Parliament and the Council Directive 2002/47/EC of June 6, 2002. *See* departementspromemoria DS 2003:38 and prop. 2002/05:30 (finansiella säkerheter).

74 *See* for instance Millqvist p. 120 and 151.

75 One example could here be mentioned with respect to Swedish law. Sec. 37 of the contract act sets out a prohibition for a lender and pledgee to request that in case of failure of the borrower to pay in accordance with the loan agreement the pledged property shall be taken over by the pledgee. This is a provision that has been in existence for a long time. This provision may cause problems in connection with project finance where so-called step in rights are often allowed the lenders. One may, however, say that in practice the rule ends up in valuation questions.

Let me here only remind of such transaction forms as hire purchase, factoring and leasing. Swedish law enacted legislation on hire purchase already almost 100 years ago (regarded as an early consumer protective piece of legislation), but presently the Consumer Credit Act applies to hire purchase where the seller is a business and the buyer a consumer and “Lag (1978:599) om avbetalningsköp mellan näringsidkare” applies to hire purchase transactions between businesses. When new transaction forms were introduced into Sweden such as leasing and factoring there were debates on whether particular legislation should also be introduced, but the Swedish legislator decided not to do so. This means that in disputes related to factoring and leasing and apart from the particular standard conditions that have been developed courts have to fall back on existing rules and general principles which have not been specifically designed for these transactions.<sup>76</sup>

#### 4.3.2.4 *Trade finance – usage and contract terms and conditions*

Some words should be mentioned regarding another type of law making, where the legislator is not involved, but where courts will have to act as interpreters and as “dispute resolvers” thereby leading the development. Of course, soft law principles may appear also within the public law field but private law seems to allow for a more flexible legal development through various forms of rules and principles.

In international commerce *lex mercatoria* has played a particular role in the legal evolution, although *lex mercatoria* principles are not always easy to define precisely. With respect to financial law *lex mercatoria* has had particular importance in the field of trade finance, in particular where documentary letters of credit and financial guarantees are involved.<sup>77</sup>

Above in 4.3.2.2 mention was made of the development of standard form documents such as the LMA and the ISDA conditions respectively, but I shall here mainly consider the use of standard terms, the development of usage, customs and soft law in trade finance.

The reason for this is not because they are fundamentally different from other private law transactions and relations, but because they have developed in particular ways slightly outside the traditional private law highways.

There are several situations where a court is facing legal problems in connection with transaction types which develop gradually. I shall here as an illustration use a particular payment device, namely the documentary letter of credit and a particular financial security device, namely the on demand guarantee. Particularly the letter of credit developed in a trading environment often without relation to a particular jurisdiction but rather tied to particular market places. The letter of credit has certain features which are similar to

---

76 This is also where for a Swedish court the various European principles drafted (such as the CFR and PECL) may serve as a source of inspiration even though not directly applicable.

77 This is an area where the International Chamber of Commerce (ICC) has played a particular role.

those of “promissory notes”<sup>78</sup>, and like the promissory note and the bill of exchange it has its roots centuries back in history at various market places. Letters of credit have, however, gradually developed to find the form which they have to-day. We can also see in legal literature and in case law how the design of the letter of credit has been discussed against the law of promissory notes, the law of agency and the law related to surety.<sup>79</sup>

As a consequence of the English dominance in trade and trade finance during the 19<sup>th</sup> and the early 20<sup>th</sup> centuries English law came to have a particular impact in these legal areas. With respect to letters of credit (as well as some other financial undertakings) the development took a particular turn which could be used to illustrate the evolution from a traditional into a modern form of “lex mercatoria”. This being said it is necessary to underline that there are still letter of credits disputes which have to be determined and decided against a background of general contract and obligatory law.

This development is embodied in the drafting by the International Chamber of Commerce (ICC) of the Uniform Custom and Practices (UCP –now 600) and the Uniform Rules on Demand Guarantees (URDG –now 758).<sup>80</sup> UCP has since the version 1962 virtually global use whereas URDG 758 seems to be gaining gradually more use but does not have global recognition. Both these sets of rules and practices are to-day probably better described as standard documents of a qualified character, and UCP has by Philip Wood been characterized as monopoly terms and conditions in that they are virtually always referred to and used when letters of credits are issued.<sup>81</sup>

The evolution of letters of credit and the rule system around them may serve as a model for the development of certain types of rules, which may also have a certain importance in relation to other modern financing phenomena. There are also complicating factors in relation to letters of credit through choice of law matters, which may arise between the different contractual parties involved in a letter of credit transaction. In other words the letter of credit may be seen as a commercially practical solution which has been tested against different legal concepts in order gradually to be established as an instrument with relatively common and generally accepted functions. This model of regulation has thus

---

78 Promissory note in English law is not exactly corresponding to “skuldebrev” in Swedish law. Often a “note of indebtedness” or similar is used in stead of a promissory note in order to minimize the risk of misunderstanding.

79 The gradual fitting of the letter of credit into the legal system has been illustrated through a large number of cases. Gorton, *Rembursrätt*, Lund 1980, from a Swedish point of departure refers to the then existing legal literature in various legal systems. For a thorough survey of legal questions related to personal security see i.a. Drobnig, *Personal security* (Principles of European law, Study group on a European civil code), München 2007.

80 UCP indicates that they have developed through custom whereas URDG rather mirrors the rules being of a contractual origine. I do not here delve into the best known ICC usages, namely the Incoterms latest version 2010, since they do not concern financial matters.

81 There is specific legislation on letters of credit only in few countries (so for instance in the US where Chapter 5 in the Uniform Commercial Code has such rules but basically used for interstate commerce only) whereas guarantees are more closely related to sureties although on demand guarantees are creatures of somewhat different nature.

evolved on a private but on truly international basis but accompanied by national case law. Come to this that case law which has developed in some legal systems seems to have been recognized to be of particular guidance value.<sup>82</sup>

#### 4.3.2.5 *Financial advice and professional negligence*

During the last 20 years period the question of financial advice and professional negligence seems to have developed particularly, also in Swedish law. Financial advice may be given separately or in connection with other transactions e.g. the sale or purchase of financial instruments. A bank may also be asked to render financial advice as a separate service or in connection with another financial service such as the negotiation for a loan agreement. This is a legal domain which has again developed earlier in many other jurisdictions but where the Scandinavian countries have during the last decade taken legislative steps particular where private persons are involved as clients. The Consumer Credit Directive and the Swedish Konsumentkreditlagen do not particularly address related questions, but following the development in case law particular consumer protective legislation was introduced through “Lag (2003:862) om finansiell rådgivning till konsumenter”. To this could be added some regulations given by the Swedish FI.<sup>83</sup>

Again EU has had an impact more generally with respect to the financial markets through the introduction of the Markets in financial investments directive 2004/39/EEC (MiFID), and Swedish legislation based on this directive was adopted through Lag (2007:528) om Värdepappersmarknaden. This piece of legislation is characterized by its relative complexity, but when adopted into Swedish law the Swedish legislator had to consider various directive solutions in relation to established Swedish law.

#### 4.3.2.6 *Some other financial transaction types and instruments*

Apart from some of these financial transactions already mentioned above in 4.3.2.3 some words should here be mentioned about certain transaction types and some new instruments. With respect to securitization there are, as far as I know, no standard contract terms, not the least due to the variation between different transactions. There are, however, models for the design of securitization set ups. In Swedish law an amendment was made into the act on promissory notes in order to facilitate securitization, but as far as I know there have not been any significant increase of securitization transactions subject to Swedish law.<sup>84</sup>

---

82 See e.g. the considerations given by the court in NJA 2002 p. 244 at p. 251 ff.

83 See about this development in particular Korling, *Rådgivningsansvar: Särskilt avseende finansiell rådgivning och investeringsrådgivning*, Stockholm 2010 with references.

84 There also seems to have been a reduction of securitization transactions as a consequence of the financial crisis connected to the “subprime-loans”.

A different type of terms and conditions with strong influence are the so-called ISDA agreements.<sup>85</sup> These agreements are generally rather complex and have been designed as a kind of “Master Agreement” with respect to various forms of derivatives.<sup>86</sup> Changes and amendments may be made in them, but this is mainly done through addenda and for that matter deletions sometimes directly in the form. Normally different “schedules” designed for the individual transaction will be attached to the frame agreement. There are different ISDA-agreements depending on whether the deal concerns a currency option, a credit derivative or an interest swap.

As we have seen above in 4.2.5 administrative law rules have been discussed and to some extent adopted, but the private law side here plays an important role, and English and American courts have been called upon in a number of disputes related to the particular financial instruments here mentioned.

## 5 Final Remarks

The above is by no means a complete list of rules or principles that have evolved during the last few decades related to financial products and markets, but they merely serve to illustrate the amount of rules which have been introduced, opening up for the question if, and then to what extent and how globalization of financial law may take place. They also illustrate how law may evolve in different ways and through different methods. I have tried to and have hopefully to some extent been able to show the interrelation between the development of administrative law and private law with respect to certain financial matters. It is obvious that there are links between them, but they have different bases and will presumably continue to develop thus.

Are there then any particular conclusions to be drawn from the above? The short and truthful reply is possibly no. Even if it could hardly be stated that there exists a truly international, let alone global financial law, there is a rather complex pattern of intertwined rules of different character and on different levels, which may be seen as pulling in the direction of a “global law” in spite

---

85 International Swaps and Derivatives Association. See e.g. Hudson, *The law of finance*, London 2009, where he discusses derivatives on p. 1088 et seq., swaps on p. 1099 et seq. and the ISDA agreements on p. 1116 et seq. See also Wood, *Law and practice*, chapters 26 and 27. Mörner, *Swappar – några Juridiska aspekter*, in *Juridisk Tidskrift* 1996-97 nr. 3 p. 649 et seq. introduced related questions into the Swedish legal literature. In Swedish law Johansson has treated related questions in *Options- och terminsavtal. En rättslig studie över handeln med standardiserade derivatinstrument*. Stockholm 1998.

In the case *Westdeutsche Landesbank Giro Zentrale v. Islington London Borough Council* /1996/ AC 669 Lord Goff gave a good account of of an interest swap transaction: “Under such a transaction, one party (the fixed rate party) agrees to pay to the other over a certain period interest at a fixed rate on a notional capital sum: and the other party (the floating rate payer) agrees to pay in accordance with a certain formula. Interest rate swaps can fulfil many purposes, ranging from pure speculation to more useful purposes such as the hedging of liabilities”.

86 Close to a kind of frame agreement.

of courts mainly being connected with their own jurisdictions. It is obvious that even in the perspective of a Swedish lawyer the legal framework around financial law matters involves so much more than Swedish law. Even when operating on the Swedish financial market financial institutions will often have to take into consideration rules which have their basis outside the Swedish jurisdiction. This is true with respect both to private law and to public law matters and even more so with respect to usages and standard documents.

If summarizing the above it is obvious that a large amount of rules have developed on different levels and in different legal spheres. Both public law and private law rules have effects for the financial markets and with respect to the players on them although these effects vary.

In a historic perspective some financial instruments have evolved outside local jurisdictions (trade finance did develop through *lex mercatoria*, although elements of it later turned into hard national law). There are thus legal elements which have multinational basis, and which have sometimes been hardened through international conventions.

On the national level there are cases where administrative rules may have an impact on the application of private law rules. Thus the breach of an administrative rule *may* have an effect on the evaluation and judgment of the diligence standard to be applied in a tort or in a contract case, although the standards developed for private law liability may not be equal to those related to public law requirements. To which extent will then the approach differ between the effects of a breach of a contractual provision or a tort law principle subject to one legal system compared to the breach of an administrative rule?

Another question that may arise concerns the question how a contract, designed in accordance with e.g. English rules, but in the individual case subject to another law, will be interpreted if a dispute arises? Will in its interpretation a court take into consideration English law surrounding the contract although English law is not directly applicable to the particular contract?

Obviously there are financial markets which are global and where several financial players act in a more or less international environment. They have to act in accordance with those rules which are applicable to them, to the particular market and to the particular transaction involved. Such rules may be international in character, even if it is not easy to substantiate generally the existence of a truly international financial law.

On the other hand it is evident that there is good ground for the statement that financial markets, financial players and financial instruments have developed and exist in an international environment, where there is need of certain common approaches and common solutions in respect of the various problems arising. The globalization of the financial activities may be a reason to call for global regulation and supervision, but it is doubtful whether such global systems will work. Personally I fear that too large systems even if created with good intentions have a tendency to be counterproductive, and there is a risk that a calamity then arising in the end will have even greater consequences and impacts.

Much new legislation in the public law sector of this legal area is a consequence of financial mishaps or financial crises, and the various legal steps

taken have been taken for political purposes also having an economic background, where the legislator is struggling with moral and economic efficiency.

With respect to loan agreements there is certainly an ongoing internationalization or globalization at least as far as trade finance and loan documentation is concerned. This does not necessarily mean that there is a globalization in case law, but courts in different jurisdictions will decide disputes in relation to the individual loan documentation. On the other hand it is important to observe that the drafting of loan documents seem to follow to a gradually greater extent a similar contract model, which may have some importance for the legal evolution in this legal area.

When used with respect to law teaching, to literature and so forth “international financial law” is recognized as a *concept*, maybe rather as a term of art than as a term of precise law (we all know what an elephant is). When using it we know basically what is meant even if there would not be any specific international financial rules immediately applicable in the particular situation.

For practical purposes that may be good enough.

