CENTRE DE DROIT
BANCAIRE ET FINANCIER

A blast from the past

Bank liability in connection with structured products issued by Lehman Brothers

Par Philipp Fischer le 12 September 2023

15 years after the collapse of Lehman Brothers and 13 years after the FINMA reports “Madoff affair and distribution of Lehman products : implications for investment advisory and wealth management activities” and “Distribution of financial products to private clients”, the collapse of the Lehman Brothers investment bank is back in the spotlight. the collapse of the Lehman Brothers investment bank is back in the spotlight of the Swiss legal scene.

Should a bank compensate a client who has suffered a financial loss in connection with structured products issued by Lehman Brothers, which the bank had advised him to purchase ? The Swiss Federal Supreme Court’s decision 4A_329 2021 of March 30, 2023 – rather curtly – answers in the negative.

The facts can be summarized as follows : two sisters from Ticino hold a joint account and, on the advice of their relationship manager, invested in structured products issued by Lehman Brothers in 2007. The collapse of the US bank in 2008 resulted in a substantial financial loss for the two clients.

Following the rejection of their action at cantonal level, the sisters lodged an appeal in civil matters with the Swiss Federal Court. In their view, the bank was liable for the loss suffered, since (i) the parties were bound by an asset management contract and (ii) the clients had not been provided with sufficient information.

Firstly, the Federal Court recalls the classic distinction between asset management and investment advice, focusing on the party making the investment decision, i.e. the financial services provider in the case of an asset management mandate, and the client in the case of an advisory mandate. In this case, the investment decision was taken by the clients, which implies an investment advisory relationship.

The appellants’ second complaint concerned the duty to inform. The Federal Court recalled that the rules governing mandates (art. 394 ff CO) apply to investment advisory contracts, and then focused on the question of compliance with the duty of care under art. 398 para. 2 CO.

- This duty requires the bank to inform the customer of all the elements essential to the formation of the customer’s will. In particular, the bank must warn the customer of the risks associated with the recommended investment.

- With regard to structured products, the Federal Supreme Court reiterates its case law (cf. in particular TF ruling 4A_624/2012, c. 2.1), according to which a structured product combines several financial instruments, such as a bond and an option, to create a new financial product. Its redemption value depends on changes in one or more underlying values. It often includes an interest-rate transaction with a derivative component. Capital-protected" products guarantee repayment of the capital invested at maturity. One of the main risks incurred by investors in this type of investment is the credit risk associated with the issuer ("issuer risk").

Applying these principles to the case in point, the Federal Court held that the risk whose materialization led to the loss suffered by the clients was the issuer risk, which did not require any specific warning from the bank and which was not inherent to the structured product (given that, for example, a bond is subject to the same risk). Furthermore, the appellants did not indicate in what way the provision of the SBA brochure "Risks inherent in trading in financial instruments" would have improved the appellants' level of information and led to a renunciation of the disputed investments.

On this basis, the Federal Court rejected the appellants' claims.

The practitioner is left wanting after reading the Federal Court's brief recitals. However, the following points are worth noting :

- Even though they are referred to (without precise citation), the Federal Court's recitals contrast with the FINMA reports mentioned in the introduction, which are among the driving forces behind the enactment of the LSFin. The FINMA report on distribution, for example, stresses that the retail investor did not necessarily understand the extent of the issuer risk, nor indeed the identity of the issuer in the case of white-labeled products : "Given that the capital protection of these products only comes into play if the solvency of the product issuers is guaranteed, purchasers of these products considered safe in principle found themselves with a loss of their invested capital" (page 33). There is no trace of the asymmetry of information observed by FINMA in the judgment commented on here.
- The Federal Court places its analysis of the bank's obligations exclusively at the time of the advice (c. 4.3.2 : "Ora, nemmeno la ricorrente afferma che il crollo della società emittente era prevedibile nel momento in cui è stata effettuata la consulenza agli investimenti"). In the context of this investment advisory mandate (it is not clear from the brief facts of the case whether this was a "global advisory" or "transactional advisory" relationship, according to the terminology currently used in articles 11 and 12 of the LSFin), the Federal Court – rightly – did not find any obligation on the part of the bank to follow up on the recommended investments and proactively warn clients at a time when Lehman Brothers' financial situation was worsening.
