

INTRODUCTION TO INTERNATIONAL FINANCIAL LAW (LL206)

Course duration: 54 hours lecture and class time (Over three weeks)

LSE Teaching Department: Department of Law

Lead Faculty: Dr Philipp Paech

Pre-requisites: Introduction to legal methods or equivalent.

Course description and learning outcome:

Introduction to International Financial Law (LL206) concerns the commercial, property and insolvency law aspects of international financial transactions. It addresses questions such as 'How is a loan contract structured, and what are its effects on the parties?', 'What are the legal elements of derivatives?', and 'How can parties mitigate their financial risk through collateral and netting in an international setting?'. In short, this course explains how financial institutions make money from entering and subsequently dispersing financial risk on an international scale. The course LL206 is therefore different from, but complimentary to, the course LL207 on International Financial Regulation, which rather concerns the limits to that activity set by the states for the common good.

The first part of the course (1 lecture) will introduce students to the financial market. The lecture explores who the different players are, their goals and business models, the types of transactions they use to achieve these goals, and the role of the law and of regulation. The academic analysis of this complex picture results in a surprising finding – there are only very few basic transaction types but they come in different guises and under different names. They are used by different types of financial institutions (banks, insurers, brokers, etc.) for different purposes (speculation, security, hedging, arbitrage). Cutting through this seemingly impenetrable thicket is the first aim of this course: the picture of the financial market will become much easier once these basic mechanisms have been understood.

The second part (6 lectures) is dedicated to the different transaction types. They are used to create the various legal effects on which the financial market is built: risk creation, risk transfer, risk mitigation. For example, such risk is created when money is 'lent', either in form of a loan, a bond, a share, or a deposit. Risk transfer concerns the question of how a player can sell on such risk, which can be quite complex in legal terms. Risk mitigation is probably the most challenging yet most relevant part of financial law: transactions are used to minimize counterparty credit risk linked to the other party's insolvency as well as market risk linked to price movements. The course will examine the different variations of risk mitigation, i.e. personal surety, derivatives, asset-backed security, collateral, and risk 'shrinking' by means of set off, netting and clearing. These transactions are the lifeblood of the financial market, and any financial activity can be reduced to these basic techniques.

The third part (1 lecture) examines how these different techniques are combined in practice to form the most complex legal structures, notably true-sale securitisation and synthetic securitisation. The course will discuss the value and risks of these structures.

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In its fourth part (4 lectures), the internationalisation of the financial market will be examined, together with the resulting legal challenges. While the market is international and capital can generally flow freely across national borders, the law is still largely national. The lack of coordination between jurisdictions leads, on the one hand, to legal uncertainty and complication, resulting in loss of efficiency and consequently liquidity. On the other hand, this situation provokes a loss of influence of national legislators over the activities of financial institutions. The financial industry, by contrast, can benefit from the patchy legal (and regulatory) landscape. First, students will learn about the fundamental rules of cross-jurisdictional transactions, insolvencies and conflict of laws. Then, specific policy areas will be examined, notably international securities transactions, international safe harbour protection and the international response to the recent financial crisis from a legal perspective.

Course structure and target students:

There will be 12 three hour lectures spread over three weeks. Back-up classes (tutorials of max 18 students) of 90min each will accompany each of them to deepen the subject covered on the previous day and to answer problem questions.

This course is designed to be of both high academic and direct practical value. It appeals to current Bachelor and Master students interested in the area or preparing for a career in financial markets as well as to practitioners wishing to broaden their horizon. It will be of particular interest for the –

- Private financial sector (compliance, legal, governmental and international affairs, etc.);
- Legal practice specialising finance;
- Government and governmental agencies (policy makers from treasuries, ministries of economy/finance/justice, etc.)
- Central banks (legal, regulation and oversight, international affairs, etc.);
- International organisation and EU organs and agencies (policy makers, legal, international affairs, etc.);
- Non-governmental organisations and advocacy groups active in the field of international financial markets;

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Since parties for their transactions often choose English law, the Common law is of great importance to the financial market worldwide. In this course, Common law and Civil law will be juxtaposed so as to allow international students to see the communalities and differences and to grasp the difficulty of combining both in the context of international transactions. The course will not be told on the basis of English statutory and Common law rules. Rather, teaching is based on broad principles, using examples drawn from Common law, Civil law and international standards. As a consequence, this course is suitable and valuable for students from all jurisdictions.

Assessment:

Assessment for the course involves a 1500 word essay which is worth 30% of the final mark and a 2 hour examination worth 70% of the final mark.

Students can also obtain a certificate of successful participation if they choose not to take the exam, provided they have regularly attended the back-up classes.

Reading and core texts:

The reading is divided into *Basic Reading* and *Further Reading*. Further reading is designed for additional reference should students be interested but is not required for successful completion of the course.

There are two texts which will be used for many of the sessions. There are a number of copies available at the LSE Library. Students might also consider purchasing one or the other.

- P. Wood, *Law and Practice of International Finance*, Sweet & Maxwell, 2008 (ca. 40 £, soft bound). This book is the first building block of the Basic Reading. Students might consider buying it.
- Market aspects: S. Valdez, Ph. Molyneux, *An Introduction to Global Financial Markets*, ^{th8} ed. (7th and 6th can also be used, but not older), Palgrave-McMillan 2015, ca. 30 £

There are a number of ongoing legislative and regulatory developments at the moment. Therefore, an updated reading list will be available shortly before the course. A course reading pack will be provided in print for free consisting of texts, materials and cases. Lecture slides and notes will be available for download during the course.

1st Part: Introduction

Lecture 1: Introduction to financial law

- What is the financial market?
- The legal side of the financial market
- The regulatory side of the financial market
- Overview of types of financial transactions
- National, EU and international law

2nd Part: The different transaction types

Lecture 2: Creating risk - Raising capital

- The nature and business of banks
- A bank's balance sheet
- Loans and interest
- Deposit taking
- Syndicated loans

Lecture 3: Creating risk II and risk transfer

- Issuance of Shares (Equity)
- Issuance of Bonds (Debt)
- Issuance of International Bonds (Eurobonds)
- Assignment
- Novation
- Other transfer alternatives

Lecture 4: Risk mitigation I – Security interests

- Security interests: pledge, mortgage, fix and floating charge
- Quasi-security: title-transfer
- Distinction between fix and floating charge under English law

Lecture 5: Risk mitigation II – Financial collateral

- Financial collateral
- Substitution, margining, right of use
- Legal advantages and drawbacks
- EU and national legislation
- Securities lending and repurchase agreements

Lecture 6: Risk mitigation III – Personal surety, derivatives

- Guarantee and indemnity
- Insurance
- Futures, options, swaps
- Credit default swaps
- Recharacterisation risk
- Standard market documentation (ISDA, GMRA, LMA)

Lecture 7: Risk mitigation IV – Set off, netting and clearing

- Basic bilateral mechanism: set off, settlement netting, close-out netting
- Importance for monetary operations, derivatives, repos, securities lending
- Close-out netting and insolvency principles
- Multilateral clearing and central counterparty clearing

3rd Part: Financial Engineering

Lecture 8: Securitisation and Asset-backed securities

- Structured finance
- Asset-backed securities
- True sale securitisation

- Synthetic securitisation
- The role of rating agencies and investment banks
- Legal risks

4th Part: Global markets and domestic legal policies

Lecture 9: Internationalisation of the Market

- Cross-border financial services, branches and subsidiaries
- Insolvency of multinational financial institutions
- Territorialism and Universalism
- Conflict of laws: Lex rei sitae, lex societatis, lex situs, lex contractus, PRIMA
- Choice of law and the global influence of English law

Lecture 10: Transfer of financial instruments

- Stock exchanges – trading of securities
- Clearing organisations – settling the trade
- Domestic holding and transfer of securities
- International holding and transfer of securities
- Derivatives clearing

Lecture 11: Financial sector insolvency – a special area of law?

- Safe harbour protection of financial institutions
- The tension between contract law and insolvency law
- Effects on systemic risk and liquidity
- Internationalisation on the basis of master agreements

Lecture 12: The Financial Crisis and financial law

- Phases of the Financial Crisis
- The role of financial law and regulation
- Bank resolution and financial law (bail-in, asset transfer and moratorium)
- The lack of an international framework
- Substitutes

Credit Transfer: If you are hoping to earn credit by taking this course, please ensure that you confirm it is eligible for credit transfer well in advance of the start date. Please discuss this directly with your home institution or Study Abroad Advisor.

As a guide, our LSE Summer School courses are typically eligible for three credits within the US system and 7.5ECTS in Europe. Different institutions and countries can, and will, vary. You will receive a digital transcript and a printed certificate following your successful completion of the course in order to make arrangements for transfer of credit.

If you have any queries, please direct them to summer.school@lse.ac.uk