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FX mis-selling moves up the agenda

by Farah Khalique

Mis-selling of derivatives is fast becoming a hot topic in foreign exchange, as industry players come under pressure from businesses, regulators and the press to be transparent on price and product. Concerned market participants are urging the City watchdog to investigate forex mis-selling and, in the meantime, are educating businesses on how to avoid sales sharks and dodgy derivatives.

The Association of Corporate Treasurers (ACT) is one such organization on a mission to support companies with their currency requirements and ensure they get the best deal on their derivatives.

ACT members include blue-chip multinationals, such as FTSE 100-listed mining company Rio Tinto, but the trade body is keen to stress it can help smaller companies too, even those that perhaps don't have a dedicated treasurer but rely on a finance controller or finance director.

Speaking at a seminar on Wednesday on forex derivatives, James Lockyer, development director at the ACT, said: "We want to let smaller businesses know we exist. If you do [derivatives] wisely you can really help the business. If you don't, you can destroy it.

"The threshold for multinational is much lower today than in the past, and our range of resources can support those working in or with companies of any size."

The right message

Banks are less enthusiastic about selling derivatives to smaller businesses, paving the way for new entrants and a wider range of tools. Robin Henry, partner in the financial services team at law firm Collyer Bristow, warns that brokers now have the pricing software to quickly price a complex derivative, making it easier for them to offer such structures to unwitting customers.

Western Union is one such new entrant that is targeting small and medium-sized enterprises (SME) with its currency derivatives offering, which has grown 30% during the past three years. [A recent Euromoney article cited a dubious claim on its website](#) that "in just two minutes" business owners can "learn how to identify the ways fluctuating currencies impact your business, set yourself a budget level and understand the amount of risk you are willing to take", simply by [watching a video on its website](#). Western Union has now redacted this claim.

"It didn't convey the right message," admits Tony Crivelli, head of Western Union Business Solutions (WUBS) for the UK and EMEA.

"We need to sell the benefit of having a face-to-face with an SME to take them through a suitability check and to get a hedging recommendation before they commit to purchasing financial derivatives."

WUBS' website is currently undergoing a rebranding, and the firm is re-evaluating its messaging to customers, says Crivelli.

Derivatives checklist

[Companies need to be mindful of a number of factors when entering into derivatives contracts](#), to



If you do [derivatives] wisely you can really help the business. If you don't, you can destroy it

James Lockyer,
ACT

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ensure they are not mis-sold an unsuitable product. These include the premium on a product – products that claim to be premium-free often have the price embedded somewhere in the contract – exorbitant break costs, should the customer wish to terminate the agreement, appropriate suitability tests and contingent liabilities.

In some instances, the bank retains the right to extend the life of a derivative, but this can have ramifications for a customer's credit limits, which need to be discussed in advance.

Also speaking at Wednesday's seminar, Abhishek Sachdev, founder of independent consultancy firm Vedanta Hedging, warned of excessive profit structures that are skewed in favour of the bank.

"The more profit the bank makes on a derivative, the worse it is for a client," he said. "Some derivatives only have a small chance of working in the client's favour."

Legal minefield

Businesses that feel they have been mis-sold a forex derivative face a legal grey area, highlighting the need to carefully understand a derivative contract before signing on the dotted line. The Financial Conduct Authority (FCA) regulates derivatives in its Conduct of Business Sourcebook, but legal action might only be brought if you are a "private person", under the Financial Services and Markets Act. This excludes most businesses.

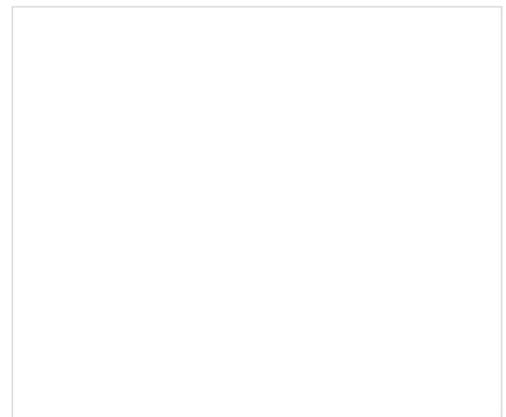
The FCA also insists firms provide clients with 'best execution', ie to sell customers products at the market rate, but this protection only applies to retail clients, not businesses. They should therefore check whether a firm has a contractual 'best execution policy' in its terms and conditions, as that could give rise to a claim for breach of contract.

Statutory protection might be limited, but claimants can look to common law, namely a bank's duty to advise and/or provide complete and accurate information to the customer. However, many banks have incorporated disclaimer clauses in their terms and conditions – basis clauses – which negate any advisory duty.

A basis clause means that, even if a bank advises a client and recommends a product, they do not have an advisory duty. However, claimants' lawyers are fighting back, arguing that these draconian clauses are in fact 'exclusion clauses', which can be deemed unreasonable and struck out under the Unfair Contract Terms Act 1977.

The validity of these disclaimers is being hotly contested in the UK courts by a [husband-and-wife business, pursuing a negligence claims against RBS](#) (Crestsign v RBS) over an interest-rate swap sold in 2007. A win for Crestsign could have massive repercussions for banking contracts; banks would no longer be able to duck responsibility for bad advice. However, their appeal hearing won't be heard until April 2016.

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