



# SKADI Impact Piece

Citi/Revlon Loan Payment Error:  
Implications for Financial Institutions

**\$500m**

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## Skadi Scores: Risk Focus

Confirmations (under NY Law)	Low	Med	High
Culture	Low	Med	High
System Bootstrapping	Low	Med	High
Payments (under NY Law)	Low	Med	High
Transaction Approval	Low	Med	High
Vendor Management	Low	Med	High

### Summary

*Citi wired the full principal plus interest to creditors, rather than the intended interest payment (\$7.8m)*

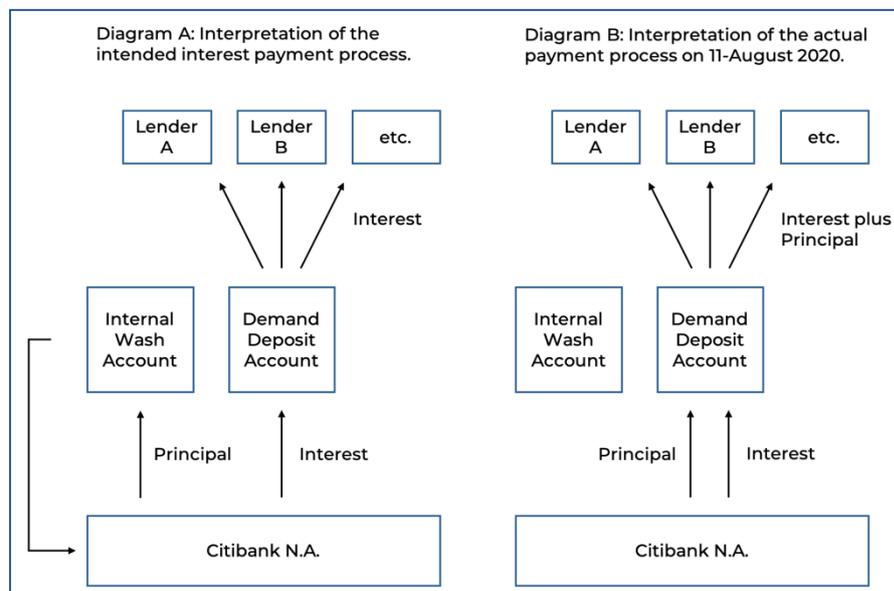
### Background

In August 2020 Citibank, acting as Administrative Agent for a loan taken out by Revlon, intended to wire an interest payment of \$7.8 million to a group of Hedge Funds but, due to an *operational mistake*, erroneously wired almost \$900 million of its own money instead. The payment occurred in connection with a "roll-up" transaction which involved exchanging positions in a 2016 Term Loan for positions in a different Revlon credit facility. Typically, when a lender "rolls-up" and exchanges a position from one facility to another, the accrued interest from the original loan is paid at the time of exchange. As this interest payment was "off-schedule" and not on a standard coupon date, an internal system had to be manually bootstrapped to generate the payment, and this is where the problem occurred. The total paid out was exactly equal to the sum of the principal loans and interest that Revlon owed to its lenders in its 2016 Term Loan. After noticing the error, nearly \$400 million was returned to Citibank, but 10 funds refused, withholding their payments totalling around \$500m. [Full court filing [here](#)]

### What went wrong?

The transactions were processed by Citibank's Asset-Based Transitional Finance (ABTF) team. On their payment system, the method for paying the lenders their share of the principal and interim interest owed was to pay off the entirety of the loan to trigger the accrued interest payments to the lenders, but then to direct the principal payment to an internal Citibank account.

*Internal systems had to be over-ridden to trigger the interest payment.*



*Transaction was checked by 3 staff members, and a system "stop sign" warning regarding funds being sent out of the bank was misunderstood.*

*As the funds were to pay off a debt, and recipient did not know it was a mistake, the payment stands.*

*Transaction approval processes need increased consideration whether internal systems can cope with new features added to financial products.*

*For transactions based on NY Law going forward, will there need to be an overhaul of transaction messaging pre-payment?*

*Documented internal procedures and training can only go so far...*

### The System Bootstrap

On 11-August, the payment details were entered into the Flexcube system by an operator at Wipro (Citi has a dedicated team at Wipro in India), with an override to ensure that the principle was sent to an internal wash account. The transfers were checked by 2 other employees under the Citibank "six-eyes" approval procedure and released to the Lenders. At approval stage, the employee clicked through the warning "stop sign" that checks for funds being sent out of the bank, as he assumed that it only referred to the interest payment leaving the firm, not the principal. The ABTF also sent the Lenders a Calculation Statement, detailing the amount of interest they were to be paid. It was not until reconciliation the next day, when a number of large "cash breaks" were discovered, that the error became known.

### Legal Findings

The court quickly established there was no doubt that the funds belonged to Citibank and were transferred by mistake. However, a United States Federal judge ruled that Citibank were not entitled to recoup their transfers, citing a 1991 case, *Banque Worms v. BankAmerica Int'l*, whereby when a beneficiary receives money to pay off a debt that it is entitled to and has no knowledge that it was wired erroneously, these funds should be considered final and not subject to revocation. This is known as the "discharge-for-value defence", and the defendants successfully argued this was applicable to this case. Citibank have said that they will appeal the decision.

### Control Implications

The case highlights a number of control implications that all financial institutions should consider going forward...

- **New Transaction Approval (NTA) Process**

In any financial institution, an NTA will need sign-off by multiple parties, including Legal, Compliance, Accounting, Front Office, Structuring, Treasury, Market Risk and Credit Risk. Given the perceived "small" amount of the \$7.8m interest payment, would any of these have considered the Operational Risks that Citi was about to expose itself to? It is common for structurers to add features to financial instruments to make them attractive - do NTAs give enough consideration as to whether these features can be effectively modelled, processed, and supported by the bank's internal systems?

- **Reconciliation**

The ABTF generated "Calculation Statements" through its local agents in India. Citibank also issued "Transfer Confirmations" via SWIFT listing the actual amounts transferred to each recipient. The fact that these 2 numbers did not match and were not picked up until cash breaks were discovered the next working day, raises questions regarding which departments have line of sight over various internal processes. Could the reconciliation have taken place before the SWIFT confirm being sent? The fact that the SWIFT confirm was sent added to the confusion and effectively helped provide some of the evidential basis for Citibank losing the case. Going forward, for instruments carrying NY Law risk, maybe there needs to be an overhaul of transaction messaging pre-payment (the judge referred to this in his conclusion).

- **Bootstrapping Systems / Manual Override**

The court papers walk through the events that happened on the 11-August in great detail and highlight the need to review processes that occur on an infrequent basis. The documents detail how Citi had a "Fund Sighting Manual" that provided instructions for suppressing Flexcube's default. The manual explains that to move funds to a wash account, the "FRONT", "FUND" and "PRINCIPAL" boxes must all be checked, but all 3 of the "six-eye" team believed that only "PRINCIPAL" had to be checked. As this shows, having a documented procedure and training in place is no defence against mistakes occurring! Financial institutions process billions of dollars-worth of transactions every year without any issues, but it might only take one small mistake on a rare type of transaction to cause a large financial loss.

*A need to revisit agreements with third parties.*

*The damaging effect poor culture has in the Financial Industry.*

#### Control Implications (cont...)

- **Offshoring of Operations / Vendor Management**  
As many banks have moved certain operational aspects of their business overseas, this case will turn a spotlight on what risks, and therefore liabilities, lie in using an outside third party? Should agreements be revisited to determine how liabilities and risks are apportioned between banks and contractors?
- **Culture**  
The court documents note that the first thing one of the clients (Allstate) discussed on receipt of the funds was *"...the possibility that Revlon and Citibank had chosen to pay off all of Allstate's clients as part of an attempt to manipulate the voting rights on the Lenders"*. This is a sad reflection on the damaging effect poor culture has had, and continues to have, on the Financial Industry. When an unexpected event arises, and the first thoughts are to the possible malign motivations a counterparty might have, it clearly demonstrates the corrosive effect poor culture has had. This also supported the decision that receivers of funds could reasonably not have determined the payment was an error, leading to the judgement given.

#### About Skadi Limited

Founded in 2012, Skadi Limited is a company focused on business integrity. We strive to help our clients improve overall efficiency utilising our in-depth market knowledge and expertise. After decades of experience gained at major global institutions, our goal is to pass on the many lessons learnt and solve problems wherever we find them.

Skadi employees are senior professionals, drawn from front-line roles in Trading, Sales, Structuring, Market Risk, Capital Markets, Finance, Operations and Research functions. Their deep understanding of market practices means the team are highly skilled in looking beyond just the data, processes, and procedures to identify and mitigate key areas of risk.

Skadi are industry leaders in complex wholesale financial investigations and also provide independent market expertise, advice and training to control function areas at regulated firms within the financial markets. The team have wide ranging product knowledge, with a number of professionals having worked in overseas jurisdictions.

Law firms regularly rely on our subject matter expertise for litigation support, dispute resolution and expert witness testimony. We also provide detailed training on a broad range of products and regulations to improve overall client understanding in a number of sectors.