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Client briefing
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Contentious Commentary

A review for litigators

Contract

Down the pan

The court takes a strict approach to the interpretation of a loan agreement.

LMA standard documents seldom reach the courts, but in *Strategic Value Master Fund Ltd v Ideal Standard International Acquisition SARL* [2011] EWHC 171 (Ch), Lewison J delved into the bowels of a senior facilities agreement, taking a strict, almost old-fashioned, approach to interpretation. (It is also interesting that the case was started in the Chancery Division rather than the Commercial Court. Perhaps the claimant hoped for an equitable interpretation. If so, it was disappointed.)

C was a small part of a syndicate that financed, just before the credit crunch, the acquisition of a group making bathroom furniture. The other syndicate members were originally major banks but, after difficulties arose on the facility, they sold their participations to entities controlled by the private equity house behind the acquisition. The private equity house formed a sufficient majority of lenders to control most decisions, save those that required unanimity.

The borrower breached its financial covenants, which would have been an event of default without an equity cure. An equity cure was provided by the borrower using money within the group to pay off certain existing obligations to other related parties. The money ultimately reached the holding company, which lent the money back to the borrower as subordinated debt. The borrower's cash position therefore remained the same but, under the definitions in the loan agreement, the indebtedness to the holding company did not count for the purposes of the financial covenants, presumably because it was subordinated. The resulting adjustment of the figures meant that the borrower complied with the financial covenants.

But, asserted C, no new money had been put into the group, which was contrary to the underlying purpose of an equity cure. Lewison J disagreed. C pointed to the Supreme Court's purposive approach to the construction of contracts in *Re Sigma Finance Corporation* [2009] UKSC 2, but the judge riposted with a reference to a case saying that a purpose must be that of both parties, not just one. The purpose asserted by C concentrated on the perspective of the lenders, and minority lenders at that. C's core problem, however, was that the agreement said that an equity cure could be effected by a subordinated loan. That was what had happened. What was there to complain about?

The next issue was whether the borrower was insolvent for the purposes of the facility agreement. The agreement provided that it was an event of default if the borrower "is, or is deemed for the purposes of any applicable law to be, unable to pay its debts as they fall due or insolvent". The borrower was incorporated in Luxembourg, where the borrower's having assets worth less than its liabilities was not a ground for its winding-up. C argued that the English law balance sheet insolvency test applied, and on that basis the borrower was insolvent.

Lewison J said that English law might be the governing law of the loan agreement, but that did not make English law an applicable law for the purposes of this event of default because the borrower did not carry on business in England. An applicable law was the law of any country in which the borrower could be wound up. As a result, the Judge said, the borrower was not insolvent within the meaning of this Event of Default.

Key Issues

- **Waiving terms, rights and commas**
- **Email guarantees**
- **Entire agreement clauses and misrepresentations**
- **Guarantees can be revoked**
- **Another misselling case fails**
- **No libel claim on letter to solicitor**
- **The risks of applying for an extension of time for service**
- **Liverpool supporters win again**
- **English contract law trumps foreign insolvency law**
- **Counter-guarantee governed by same law as guarantee**
- **Champerty lives for lawyers**
- **No fixed sum costs**
- **Third party disclosure can be ordered for enforcement purposes**
- **No permission required for affidavit contempt proceedings**

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A problem with this construction is the punctuation of the clause. The commas indicate that the applicable law is relevant to deemed insolvency, but that the question of what test should be applied to determine whether the borrower is in fact insolvent is a matter of construction of the agreement rather than of any applicable law. Given the distinction in the clause between cash flow and insolvency, a more obvious construction might have been that the parties intended a balance sheet approach to be taken.

The next point was the effect of a notice calling an event of default that placed the loan on a demand basis. Lewison J decided that the existing repayment schedule remained in place, the lenders' ability to make a demand at any time being an additional right, not a right that replaced the existing repayment obligations.

The final point (obiter) was whether the majority of lenders could withdraw, or waive, a notice calling an event of default or whether withdrawal required unanimity. Prima facie, a majority could waive the event of default, but C pointed to a clause that required unanimity to waive a "term" of the agreement that involved an extension of maturity of the loan, which C said this waiver did.

Lewison J decided that this clause was not engaged at all. The agreement distinguished, he said, between a waiver of a breach, of an event of default, of a right or remedy and of a term. The clause C relied on only applied to the last kind, namely waiver of a term. Since the term in question remained available for future use, the term had not been waived. What had been waived was the right or remedy or an event of default arising from a particular breach the term. A majority was enough for that.

All interesting, fairly literal stuff. Doubtlessly, the parties using the LMA's forms will consider whether the decision accords with what they intend.

e-guarantees

The court takes a commercial approach to a guarantee agreed by email.

Email chains are often more like conversations than letters. The earlier parts of the chain remain attached, and one email builds on the next in relative informality. As a result of this, in *Golden Ocean Group Ltd v Salgaocar Mining Industries PVT* [2011] EWHC 56 (Comm), Christopher Clarke J was able to conclude that a contract had been entered into by email, and since it had been "signed", ie a name typed at the bottom, by brokers with authority, that was enough to enable a guarantee to be enforced under the Statute of Frauds 1677 (though, since this was for jurisdictional purposes, he only decided that there was an arguable case). The chain didn't end with a neat email referring to the guarantee, but the guarantee had been mentioned earlier, and when the terms of the underlying deal were finalised, the overall deal incorporated the guarantee.

The judge also decided that a claim for breach of warranty of authority against the person who had instructed the brokers to agree to the guarantee was a claim in contract for the purposes of the Rome Convention (now the Rome I Regulation). The guarantee might be subject to English law, but the individual concerned was resident in India, and the company for whom he purported to act was Indian. That persuaded the judge that any warranty of authority should also be governed by Indian law.

Entirely useless

Entire agreement clauses do not block liability for misrepresentations.

Boilerplate is the stuff at the end of a contract that no one looks at - until a dispute has arisen and it is too late to change it. So when C sought to collect sums due to it, and D responded with allegations of misrepresentation, C searched in vain for a *Springwell*-like no representation clause. The best it could come up with was the entire agreement clause. This mentioned representations, but, like Ramsey J in *BSkyB Ltd v HP Enterprise Services UK Ltd* [2010] EWHC 86 (TCC), the Court of Appeal in *Axa Sun Life Service plc v Campbell Martin Ltd* [2011] EWCA Civ 133, decided that a typical entire agreement clause prevents collateral contracts arising but does not exclude liability for misrepresentation. The sting for D was that Stanley Burnton LJ said that it looked as if most of the representations pleaded were not representations of fact but rather advice or collateral warranties, which might therefore fall within entire agreement clause.

C went on to argue that the entire agreement clause also ruled out implied terms. Stanley Burnton LJ considered that because the alleged ground for implication was business efficacy, the entire agreement clause did not preclude the implied terms alleged. The term thus implied was intrinsic to the agreement rather than being something outside it. However, he considered that if the implication was alleged to follow from something extrinsic to the agreement, it would be excluded by an entire agreement clause.

Treating an implied term as part of the agreement is in line with Hoffmannite reinterpretation of implied terms in *Belize Telecom* [2009] UKPC 10, but indicating that there might be more than one basis of implication is decidedly not. The idea that an implied term could come from outside the agreement, rather than being what a reasonable person would understand the agreement to mean, is on highly dubious theoretical ground.

Then there was reasonableness. The Court of Appeal decided that an entire agreement clause is not an exclusion clause that would normally fall within the realm of the Unfair Contract Terms Act 1977. However, since the contract was on D's standard written terms, section 3(2)(b)(i) of UCTA applied, ie it was a clause that might enable D to render performance substantially different from that which was reasonably expected of it. Representations made before the contract was entered into were relevant in determining what was reasonably expected of a party, and excluding those representations from having contractual effect was subject to a reasonableness test. However, the clause was reasonable in the circumstances. C, as a business, ought to have known that the clause was there, and it is

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sensible to agree in writing what warranties are being given rather than to rely on oral collateral warranties.

The Court of Appeal also confirmed that a no-set off clause is subject to UCTA (*Stewart Gill Ltd v Horatio Myer & Co Ltd* [1992] 1 QB 600), and decided that it was unreasonable in this case. It was unreasonable because it was one-sided: it allowed D to set off what it wanted against sums D owed to C, but prevented C from setting off anything against sums that C owed to D.

Revoking guarantees

A guarantor can revoke as guarantee going forward, unless the guarantee says otherwise.

Guarantees usually state that they are irrevocable. Most people probably think that this is typical legalistic verbiage, but *Close Brothers Ltd v Pearce* [2011] EWHC 298(Comm) shows that this ain't necessarily so. Guarantees continue until revoked but, depending on the terms of the instrument, a guarantor may revoke the guarantee, as regards future debts, unilaterally: *Silverburn Finance (UK) Ltd v Salt* [2001] 2 All ER (Comm) 438. Further, while it is necessary for a guarantee to be in, or evidenced in, writing, a revocation can be entirely oral. This happened in *Close Brothers*, which lost the ability to call on its guarantee.

Tort

Déjà vu all over again

Misselling claims continue, but customers operating under execution-only arrangements are still finding it difficult to show that they were owed advisory duties.

Wilson v MF Global UK Limited [2011] EWHC 138 (QB) has a familiar ring to it. C was a successful businessman who opened a series of accounts with D so that he could trade in contracts for differences, futures and options and indulge in spread betting. He incurred losses through his trading, but then asserted that they were not his fault. He sued D, claiming damages of over £1 million.

The accounts were all opened on an "execution-only" basis. C was given the use of trading platforms that enabled him to conduct his own trades and he had real-time information on his trading positions. However, he had regular telephone conversations with D's trading desks, and hundreds of conversations with one broker, who was designated as his account handler. C asserted that the broker's discussion of market conditions and particular investments meant that the relationship was an advisory one, and that D had not given him proper advice.

The court dismissed the claim, noting that the contractual documents made it clear that D was under no duty to give advice. D was entitled to provide market information, advice and recommendations, but the documents stated that any such advice would be regarded as incidental to the dealing relationship, which was non-advisory in nature. A reasonable client in C's position would have understood that he was not being given advice on the merits of particular transactions, but that D had discretion to give market information and recommendations in the context of an execution-only dealing relationship.

The court also dismissed C's argument that he had been incorrectly classified by D as an "intermediate customer" for the purposes of the FSA's Conduct of Business rules. C had argued that he should have been classified as a private customer, which would have meant D owing him a duty of suitability in respect of personal recommendations given to him (although the court also found that there had been no personal recommendations).

Clifford Chance LLP acted for the defendant in this case.

For your eyes only

A defamatory statement made to the defamed's solicitors is struck out as an abuse of process.

A defamatory statement only has to be published to one third party in order to give a claimant a cause of action. In *Wallis v Meredith* [2011] EWHC 75 (QB), that is exactly what happened. D wrote to C's lawyer, noting that, after a falling-out with C, D had been visited by "two burly men with East European accents who threatened me and told me to 'phone the man who you have offended and say sorry'." C sued for defamation, but D applied to have the claim struck out as an abuse of process, based on the decision of the Court of Appeal in *Jameel v Dow Jones Inc* [2005] EWCA Civ 75, [2005] QB 946, in which a defamatory statement online had been viewed by only five people in this jurisdiction.

The Court of Appeal said that the court is required to stop as an abuse of process defamation proceedings that do not serve the legitimate purpose of protecting the claimant's reputation, which includes compensating the claimant only if that reputation had been unlawfully damaged. The test was whether there was a real and substantial tort committed within the jurisdiction. In *Wallis*, Christopher Clarke J held that there had been no real and substantial tort: "It does not seem to me that the [C] requires vindication in respect of such a publication to a solicitor who has been busily engaged in stating that the allegation is false; and that any "vindication" by success in the action will be illusory or, at best, minimal."

The judge also accepted the argument that solicitors are routinely the recipients of defamatory imputations about their clients, since most allegations of unlawful conduct are likely to be defamatory, and that such publication is likely to be covered by qualified privilege on the basis of a common and corresponding interest. This should come as a relief to the legal profession because many solicitors who act for losing parties could otherwise be subject to defamation claims.

Conflict of laws

Give them an inch

An application for an extension of time may allow forum non conveniens in by the back door.

The facts of *Katsouris Brothers Ltd v Haitoglu Bros SA* [2011] EWHC 111 (QB) are as glutinous as the salmonella infected (allegedly) tahini paste the case

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concerned. It was a battle between the Greek and English courts, which came down to whether the judge should extend the time for service of the Particulars of Claim. If he did not do so, the English claim would be struck out, the English court would no longer be seised, and the Greek courts could take over.

The judge decided not to extend the time for service of the Particulars. C therefore lost the benefit of having seised the English court first. The facts that led the judge to this conclusion were extreme, and are unlikely to be repeated, but there is a warning that even if the English court is first seised of a claim, there is a risk that, if it then has a discretion (eg to extend the time for service of the claim form or Particulars), concepts of forum non conveniens can creep in the back door even though they are repugnant to the Brussels I Regulation.

Bayat v Cecil [2011] EWCA Civ 135 also shows the perils of an application for an extension of time, in this case for service of the claim form. The facts, again, are egregious in that the extensions granted were numerous, the reasons given insufficient (searching for funding for the claim) and the limitation period passed during the period. The Court of Appeal took the hard line that an extension of time for service should only be granted if there is good reason to do so. It also emphasised that because applications for an extension are made ex parte, orders made can subsequently be set aside on the application of the defendant when service is eventually effected.

As a result, if a claim form is issued in order to seise the English courts lest the defendant seise any other court in the EU (ie to defeat an Italian torpedo) but the claim form is not served, the Court of Appeal's strict approach doubles the risk of applying for an extension. Article 30(1) of the Brussels I Regulation, which states that an English court is seised on issue "provided that the plaintiff has not subsequently failed to take the steps he was required to take to have service effected on the defendant", is a problem in itself. The claimant has the normal four/six months to serve, but an extension might be treated as falling foul of the proviso if the claimant simply doesn't want to effect service yet (service at the end of normal period is fine: *UBS v Kommunale Wasserwerke Leipzig GmbH* [2010] EWHC 2566 (Comm)). *Bayat* adds the further risk that, even if that problem can be surmounted, a court may subsequently set aside the extension, thereby unseising the English court.

Carrion crowing

Universality of insolvency proceedings is not global - yet.

The law applicable to a contract determines when an obligation has been extinguished (article 12(1)(d) of Rome I). But what if the insolvency law applicable to one of the parties purports to extinguish a contractual obligation? Clearly if legislation binding on the English courts allows that (eg under the EU Insolvency Regulation), so be it. But what scope do judges have to override the governing law chosen by the parties in pursuit of the purity of a universal insolvency regime?

There is a strong movement amongst judges in favour of their creating universal insolvency rules notwithstanding the (failed) international attempts to do so (eg *Rubin v Eurofinance* [2010] EWCA Civ 895, which swept away an established rule on the enforcement of foreign judgments in favour of universality, and which is to go to the Supreme Court). How far can or should this

Conflict of laws

Red rose of Texas

The Liverpool FC litigation has some way to go yet.

Liverpool FC has been sold, Roy Hodgson has been sacked and Fernando Torres gone, but the past cannot be forgotten that easily. The litigation that bloomed with such vigour in October may have entered a more restful phase, but it remains verdant.

In *The Royal Bank of Scotland plc v Hicks* [2011] EWHC 287 (Ch), Floyd J allowed RBS and Sir Martin Broughton to amend their claims to seek negative declarations to the effect that they have no liability to Liverpool's former owners, Messrs Hicks and Gillett. Floyd J recorded that the old suspicions about negative declarations have gone and the only question is whether a declaration is useful in the particular circumstances - "[w]ill the declaration be the equivalent of shouting in an empty room, or is there some point in it", as Pumfrey LJ put it in *Nokia Corporation v Interdigital Technology Corporation* [2007] EWHC 3077 (Pat). Given the serious allegations that Messrs H&G had made, Floyd J was satisfied that there was some point in allowing the claimants to seek negative declarations.

The judge also continued the anti-suit injunction against H&G, granted after they had leapt from defeat in the English court to the refuge of the Dallas court. The judge in Dallas had, indeed, asked why the application before him was not being made in England. He was told by H&G's lawyers that the English courts were shut, conveniently forgetting that, even if that had been true, H&G had already sought in England, but been refused, the relief they wanted in Dallas. In the light, doubtless, of this conduct, Floyd J concluded that there remained a threat that H&G would issue proceedings in Texas that were either in breach of a jurisdiction clause in one or more of the various agreements or which would be oppressive or vexatious. The injunction allowed H&G to seek the permission of the court if they wanted to start proceedings outside the EU. The judge considered that was better that way round than to accept H&G's offer of an undertaking to give seven days' notice of their intention to do so, making the C's apply to stop them doing so.

The one concession to H&G was that the judge varied the injunction to allow them to apply to the US courts to seek disclosure in support of the proceedings in England under USC §1782. Those with a presence in the US, might care to beware.

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movement go? In *Global Distressed Alpha Fund 1 Limited Partnership v PT Bakrie Investindo* [2011] EWHC 256 (Comm), Teare J recognised the judicial tide but decided that it did not allow him, as a first instance judge, to ignore a long line of binding authority.

An Indonesian company issued bonds guaranteed by D. The issuer later defaulted, and underwent reconstruction under Indonesian insolvency law, which resulted in its liability on the bonds being discharged. Years later, a fund specialising in distressed debt bought some of the bonds, and sued the guarantor. The guarantor argued that the underlying debt had ceased to exist, so there was nothing left to guarantee.

But, said the fund, the bonds and the guarantee were governed by English law. The traditional rule in English law is that, outside the EUIR, a discharge from a debt granted by foreign insolvency law is ineffective if the debt was created by a contract governed by English law (*Dicey, Morris and Collins*, rule 200, and cases going back at least 120 years). The guarantor fulminated that such a rules was Anglo-centric, outdated and, in the light of *Rubin* and its forebears, should be excised from English law.

Teare J expressed some sympathy with D, but decided that he was bound by the century of decided cases directly on point. Higher courts might re-write the law, but he could not.

Syrian rising

A counter-guarantee is governed by the same law as the guarantee.

Bank A (a Syrian bank) gives a bank guarantee that is expressly governed by Syrian law. Bank B (an English bank) gives Bank A a counter-guarantee covering Bank A's liability on its guarantee, but the counter-guarantee has no express choice of law. Bank C (a Chinese bank) gives Bank B a counter-counter-guarantee for Bank B's liability to Bank A, which counter-counter-guarantee is expressly governed by English law. What law governs the counter-guarantee?

In *British Arab Commercial Bank plc v Bank of Communications* [2011] EWHC 281 (Comm), the answer depended on the Rome Convention, rather than the Rome I Regulation, but the answer would probably not differ under the Regulation. Absent a choice of law by the parties (and Blair J decided that there was no implicit choice), the governing law is that of the domicile of the party which is to effect characteristic performance. That was Bank B, since it was the payer, which pointed to English law. But English law does not apply if it appears from the circumstances as a whole that the counter-guarantee is more closely connected with another country. Blair J decided that the counter-guarantee was more closely connected with Syria, following authority that indicated strongly that a counter-guarantee should be treated as subject to the same law as a guarantee . This led to Syrian law. (Indeed, the UK insisted on recital (20) to the Rome I Regulation to make the point that connected contracts should be governed by the same law, though it had in mind ensuring that counter-guarantees were governed by English law, rather than the reverse, as here.)

In fact, it didn't matter. Blair J decided that Bank B had no liability under either English or Syrian law, though Syrian law was distinctly less helpful. But the moral is to include an express choice of law in order to avoid tense and expensive argument on the point.

Costs

Is this a dagger which I see before me?

Champerty lives for lawyers, but should not be extended.

Champerty should be given a decent burial. Parliament may have the chance to do so with the possible implementation of Jackson LJ's proposals on costs in the not too distant future (the Ministry of Justice's Consultation on this has just closed). Whether they will get there is not yet clear, but the courts have passed up another chance to do the deed themselves in *Sibthorpe v Southwark London Borough Council* [2011] EWCA Civ 25.

Sibthorpe concerned solicitors who brought a housing disrepair claim against D on behalf of one of D's tenants. The solicitors acted on a conditional fee agreement, but also agreed to indemnify the tenant against any adverse costs order. The claim was settled on terms requiring D to pay the tenant's costs. Eureka, say D on getting hold of the CFA. The indemnity renders the otherwise valid CFA champertous, as a result of which the agreement between tenant and solicitors is unenforceable. C has no liability in costs to its solicitors, so D has no liability in costs to C.

The Court of Appeal meditated on the nature of champerty before deciding that there remained an absolute bar on those who conduct litigation (ie solicitors and barristers) having an interest in the outcome of the litigation, unless permitted by statute. This was for two reasons. First, because lawyers have duties to the court, an interest in the outcome of a case may give rise to a conflict of interest and duty. Secondly, because Parliament has intervened in the area by allowing CFAs, the judiciary should cease to develop the law significantly themselves. The Court of Appeal also considered that there was advantage in the certainty of an absolute rule rather than the uncertainty of the rule that applies to the rest of the world, namely whether the agreement in question tends to corrupt public justice.

But that wasn't enough for D to win. The Court of Appeal explored whether the indemnity in the agreement was in fact champertous. The solicitors would not receive a share of C's winnings, but were interested in the outcome of the litigation because they would pick up the downside if the case was lost. All the agreements cited to the Court of Appeal that had been found to be champertous involved someone getting a share of the spoils rather than merely covering the loser's costs. The Court of Appeal was not prepared to inter champerty, but nor was it prepared to expand champerty's scope. As a result, the Court of Appeal decided that the indemnity was not champertous.

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The Court of Appeal also decided that the indemnity did not render the CFA a contract of insurance. That would only be so if the principal object of the contract was the provision of insurance. The principal object in this case was the provision of legal services.

Finally, the Court of Appeal decided that it was possible to have champerty without maintenance. Champerty has historically been considered to be a subspecies of maintenance, with the added, and aggravating, element of receipt of a share of the proceeds. The Court of Appeal considered that the law of maintenance has withered (so, eg, third parties can fund litigation), but by keeping the rule that lawyers cannot conduct litigation in return for a share of the proceeds, there can now be champerty without maintenance.

So, generally, a mess, but the right answer. Champerty remains alive, just, as far as lawyers are concerned, but its relevance for the rest of the world seems to be nearly at an end.

Fixing the outcome

A costs order cannot be made for a fixed sum.

CPR 44.3(6) lists the costs orders that the court can make, including, at (b), "a stated amount", alongside the more usual "proportion of the other side's costs" and costs "from or until a certain date". In *Morgan v Spirit Group* [2011] EWCA Civ 68, C claimed £40k plus interest on a personal injury claim, but the judge awarded C only £13k, including interest. He thought the claim was exaggerated, had been conducted oppressively (by C's husband, a solicitor), and should have been brought on the fast track. When C asked for costs of £99k (including a success fee), the J was unimpressed, and, (probably) using the power in CPR 44.3(6)(b), sliced it to £25k.

When this got to the Court of Appeal, it was agreed that the judge had not conducted a detailed or a summary assessment of costs. He had simply come up with a figure he thought reasonable. The Court of Appeal was clear that he could not do that. He had to do a summary assessment, though it could be rough and ready, or order a detailed assessment. Plucking figures out of the air based on his experience was not acceptable, even though it seems to be what CPR 44.3(6)(b) contemplates.

Courts

Enforcing third party disclosure

Third parties can be ordered to give disclosure in support of attempts to enforce a judgment.

In *North Shore Ventures Ltd v Anstead Holdings Ltd* [2011] EWHC 178 (Ch), C sought third party disclosure under section 34(2) of the Senior Courts Act 1981 and CPR 31.17 in support not of a substantive claim but in order to elicit information about the Ds' assets so that C could seek to enforce the judgment it had already obtained. The third parties in question were the Ds' spouses, who argued that there was no power to order third party disclosure for enforcement purposes. Floyd J disagreed. He considered that the power in the CPR extended beyond the substantive claim, and that, in his discretion, he should make the order sought.

Spot the difference

Permission is needed to bring contempt proceedings based on a false witness statement, but not on a false affidavit.

CPR 32.14 allows proceedings for contempt of court to be brought against someone who makes a statement of truth without an honest belief in its truth. Proceedings may be brought only by the Attorney General, or with the permission of the court. But in *Hydropool Hot Tubs Limited v Roberjot* [2011] EWHC 121 (Ch), in which C wanted D committed for contempt for lying in an affidavit, Arnold J confirmed that CPR 32.14 had no application to an allegation of contempt by knowingly swearing a false affidavit. This activity has always rendered the maker liable to be prosecuted for perjury (because it is the equivalent of testimony on oath) and it is also a contempt of court, and the sanctions for contempt remain available in an appropriate case.

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