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Litigation and Dispute Resolution

Review

EDITORIAL

In this edition we cover six cases of interest from the end of last year including an important decision of the Court of Appeal in *Cavendish Square Holdings BV & anr v Makdessi* (see **Contract**) which focuses on the law of penalties. After an extensive review of the case law, the Court of Appeal restated the general principles to be applied under English law when assessing whether or not a clause is penal. We also include an article by Philip Annett and Victoria Gore which identifies the key issues for litigators in the new Banking Reform Act (see **Regulatory**).

We also look back and reflect upon some of the most interesting judgments from 2013 and provide our selection of decisions relevant to litigators and transaction lawyers operating in the financial markets (see **Top decisions**).

Finally, looking ahead, there are some important commercial cases scheduled for trial in the English courts in 2014. The trial started this month in *Berliner Verkehrsbetriebe (BVG) Anstalt Des Öffentlichen Rechts v JP Morgan Chase Bank NA & anr*, one of two important cases concerning the enforceability of swaps entered into by German public entities (the other case being *UBS and Depfa v Kommunale Wasserwerle Leipzig*). Certain of the issues to be determined, in particular claims regarding the capacity/authority of the entites to enter into the swaps, echo the *ultra vires* arguments raised in proceedings brought in England (and elsewhere) involving Italian municipalities that had also entered into swap transactions. Two cartel damages claims (*Cooper Tire & ors v Dow Deutschland* and *National Grid & ors v ABB*) are also scheduled for trial this year and which may result in new law concerning how to calculate cartel overcharges in antitrust damages claims.

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Arbitration

ANTI-SUIT INJUNCTION GRANTED TO PROTECT ARBITRATION AGREEMENT EVEN THOUGH NO ARBITRATION: *AES* APPLIED

Boris Bannai v Eitan Shlomo Erez (*Trustee in Bankruptcy of Eli Reifman*) [2013] EWHC 3689 (Comm), 26 November 2013

The English Commercial Court denied an application to set aside an anti-suit injunction restraining the defendant from pursuing litigation against the claimant in Israeli courts, where the agreement between the parties contained an arbitration clause.

Under an agreement between the claimant, Mr Bannai, and a bankrupt individual, Mr Reifman (the **Bankrupt**), in 2002 (the **Agreement**) Mr Bannai was to account to Mr Reifman for 35% of the assets identified in the Agreement as well as 35% of the income derived from those assets. Mr Bannai allegedly failed to make the required contributions in breach of the Agreement. Mr Erez (the **Trustee**) filed a lawsuit against Mr Bannai in the Israeli courts alleging a breach of the Agreement, notwithstanding the fact that the Agreement, governed by English law, contained an arbitration clause with London as the seat of arbitration. The Agreement specifically provided for arbitration of "*any differences of opinions and/or disputes* [of] *whatever type or kind between the Parties and/or between the JVC and/or the Parties' Family Members (hereinafter: "the Dispute"), including in relation to the interpretation and application of the Agreement.*"[1] It was common ground between the parties that the dispute fell within the arbitration clause.

The Israeli District Court refused to grant a stay. At the same time, the claimant commenced proceedings in England requesting an anti-suit injunction on account of the arbitration clause. An injunction was granted by Walker J on 31 July 2013 on the grounds that "*the Israeli court having refused a stay pending arbitration, there was an imminent breach of the arbitration agreement contained in the English contract, by which the Trustee was bound as standing in the shoes of the Bankrupt, and which should be restrained*".[2] The injunction was extended by Hamblen J on 9 August 2013 to also prevent court proceedings in Israel against Mr Bannai's son, David Bannai, and various companies.

Mr Erez applied to discharge the injunction, which was rejected by Burton J on 26 November 2013. Burton J's judgment is interesting for its analysis and application of the Supreme Court's decision in *AES Ust-Kamenogorsk Hydropower Plant LLP v Ust-Kamenogorsk Hydropower Plant JSC* (covered in the August/September 2013 Litigation Review).[3] In that case the Supreme Court found that an arbitration clause contains a negative promise not to bring foreign proceedings, which applies and is enforceable regardless of whether or not arbitral proceedings are on foot or proposed.[4] The Supreme Court held that the courts have broad powers to order anti-suit injunctions to protect arbitration clauses under s37 of the Senior Courts Act 1981. Accordingly, it upheld an anti-suit injunction even though AES had not commenced arbitral proceedings nor contemplated doing so.

Following the Supreme Court's decision in *AES* Burton J held that the negative obligation not to bring foreign proceedings is implied in a positive obligation to arbitrate disputes. A claimant does not need to even contemplate bringing arbitral proceedings: "*he is simply entitled to restrain proceedings being brought against him otherwise than by arbitration*".[5]

Burton J saw no reason why the dispute should not be resolved by arbitration. He rejected the Trustee's argument that, as the dispute concerned insolvency proceedings, under Israeli law the Trustee could

disclaim the Agreement, including the arbitration clause. He stated that: "*it is unlikely that this would be a case in which the Israeli court would uphold an application to disclaim if it were made (…)*"[6] Burton J noted in this regard that the question of disclaimer had not arisen in the Israeli proceedings and the Israeli court had not refused a stay on this basis.

The Trustee's *forum non conveniens* arguments were also discarded, as they are not normally relevant in anti-suit injunction proceedings particularly where there is an exclusive jurisdiction clause or an arbitration agreement. The additional fees that would accrue due to arbitration in London did not make arbitrating onerous: significant costs could have been saved if the arbitration clause had been respected at the outset. The inconvenience caused by the Bankrupt being imprisoned in Israel could be mitigated by other means and did not amount to onerousness. Similarly, allegations of fraud by Mr Bannai did not affect the validity of the arbitration clause or proceedings.

In conclusion, Burton J continued the original injunctions granted by Walker J and Hamblen J, which covered David Bannai as a family member as well as the various companies in order to prevent the arbitration clause from being frustrated or circumvented.

COMMENT

This case is significant in its treatment of *AES v Ust-Kamenogorsk* as clear, established law. It cements the position under English law that an anti-suit injunction can be granted where arbitral proceedings have not been commenced or where the applicant does not even intend to commence arbitration. On the basis of *AES* and *Bannai*, it appears that the English courts are likely to exercise this discretion in particular where the foreign courts have declined to stay proceedings contravening an arbitration clause. The judgment also confirms the jurisdiction of English courts to extend an anti-suit injunction to protect related parties from litigation to safeguard the efficacy of an arbitration clause.

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1 *Bannai v Erez (Trustee in Bankruptcy of Eli Reifman)* [2013] EWHC 3689 (Comm), at paragraph 13.

2 *Ibid.*, at paragraph 10.

3 [2013] 1 WLR 1889 S.C.

4 *Bannai v Erez*, at paragraph 3.

5 *Ibid.*, at paragraph 12.

6 *Ibid.*, at paragraph 22.

Conflict of laws

INDIRECT OR SECONDARY DAMAGE IN ENGLAND SUFFICIENT TO MEET TORT JURISDICTIONAL GATEWAY TEST

Pike and Doyle v The Indian Hotels Company Ltd [2013] EWHC 4096 (QB), 19 December 2013

Indirect or secondary damage in England is sufficient to meet the jurisdictional gateway test for tort claims in the Civil Procedure Rules. Although India was the "*natural forum*", or that which had the most real and substantial connection with the claim, and Indian law was likely to be the governing law of the claim, justice required that the English proceedings should continue in view of the approximately 15-20 year delay involved in bringing the claim before the Mumbai High Court.

Background

The British claimants were injured while trying to escape the terrorist attack on Taj Mahal Palace in Mumbai on 28 November 2008. The first claimant suffered severe spinal injuries and the second claimant suffers from continuing psychiatric consequences. The claimants sought to bring claims in England against the defendant, the Indian company which operated the hotel, in negligence. The defendant made an application that the English court had no jurisdiction to try the claim. Despite the seriousness of the injuries of the first claimant relative to the second claimant, Stewart J dealt with both claimants as if they were one. Neither party sought to persuade the judge otherwise.

What is the jurisdictional basis for the claims?

Jurisdiction over defendants domiciled outside the EU (and outside the Brussels/Lugano regimes) is governed by the common law regime, in particular CPR 6.36 and 6.37 with service out permitted under "gateways" in Practice Direction 6B. Under CPR 6.36 "*the claimant may serve a claim form outside of the jurisdiction with the permission of the court if any of the grounds set out in paragraph 3.1 of Practice Direction 6B apply*". The grounds or gateways include paragraph 3.1(9)(a) if "*a claim is made in tort where damage was sustained within the jurisdiction*". The claimants needed to satisfy the court that there was both a serious issue to be tried on the merits (which was not disputed) and a good arguable case that the claimant fell within paragraph 3.1(9)(a).

The claimant argued that "damage" should be interpreted widely and the fact that the claimants suffered indirect or secondary damage upon their return to England (in this case continuing pain, loss of amenity and loss of earnings) was sufficient to found jurisdiction. The defendant argued that paragraph 3.1(9)(a) applied to direct damage only (which in this case was suffered in Mumbai) and this was in keeping with European authorities and Article 5(3) of the Brussels Regulation.

Stewart J referred to a number of High Court decisions and followed Teare J's judgment in *Booth v Phillips* [2004] which determined that the ordinary, natural meaning of "damage" included physical and economic damage and that it was sufficient that some (though not all) damage was sustained within the jurisdiction to satisfy gateway 3.1(9)(a).

Stewart J said that damage should not be construed in the same way as the Brussels Regulation because European jurisdiction schemes were fundamentally different from the common law in terms of policy and structure, and the common law rules in the CPR conveyed greater discretion and flexibility.

Are the English courts the *Forum Conveniens*?

Pursuant to CPR 6.37(3), the court "*will not give permission unless satisfied that England and Wales is the proper place in which to bring the claim*". Although the claimants conceded that India was the "*natural*

forum", ie that with which the action had the most real and substantial connection, following the decision in *Spiliada Maritime Corp v Cansulex Ltd*[1987] 1 AC 460, they argued that the English proceedings should not be stayed in the interests of "justice". The defendant argued in favour of the trial taking place in India because, amongst other reasons: (i) Indian law is the applicable law; (ii) the breach of duty had to be tested against local standards in India; and (iii) there will be evidential difficulties for the defendants if the case proceeded in England (including that a large number of witnesses would require visas).

Stewart J considered that the factors in favour of a trial in India were outweighed by the 20-year delay that was likely to be involved if proceedings were brought in India. Oral evidence was heard from two Indian lawyers on the delay and the judge referred to a passage in a decision of the Indian Supreme Court from August 2013 which referred to the excessive delays in the Indian court system and stated that "*for a long time, the people of this nation have been convinced that a case would not culminate during the lifetime of the litigant and is beyond the ability of astrologer to anticipate his fate*" *Suo Motu* Contempt Petition No 312 of 2013 in Civil Appeal No 1398 of 2005.

Stewart J accepted that the case was likely to take 15 years in the Mumbai High Court and a further five to six years on appeal. The judge considered that expedition was unlikely and a delay of this magnitude would amount to a "denial of justice". This factor alone was sufficient to allow the claims to continue in England but it was given extra force because the claimants would not be able to litigate in India through lack of funding The claimants had a CFA in England and the English system provides interim payments to the claimants. Stewart J also considered that some evidence could be given "on commission" through a judge in India and that it was perfectly possible for an English judge to make a site visit to the Taj Mahal Palace.

Should the order extending time for service of the claim form be set aside?

Stewart J decided that the application to set aside the extension of time should fail. There were good reasons to justify the failure to serve the claim form in time. In particular, and amongst other reasons, the claimants did not ascertain that there were "i*mmense problems in serving process in India*" until Senior Master Whitaker in the Foreign Process Section told them of his experience. Master Whitaker advised that it could take eight months for the Indian National Authority to serve proceedings on its nationals after receiving a request from London.

COMMENT

The decision provides useful guidance in relation to the scope of the jurisdictional gateways for tort claims in paragraph 3.1 of Practice Direction 6B. In particular, the judgment adds to the already well-established case law in favour of a wide interpretation of "*damage*" to include indirect and secondary damage.

Expert evidence from two Indian lawyers regarding the likely delay in India was important in this case. The judge emphasised that their opinions should preferably be supported by proper evidence and statistical information and it was notable that the "*gut*" feeling of the defendant's expert was not considered a basis which the judge found reliable.

Stewart J showed greater inclination than judges in other recent cases to acknowledge a risk that justice might be unavailable in a foreign court. The judge considered that the extensive delays in the Indian court system amounted to a "*denial of justice*". While this judgment was in respect of the Indian courts, it is likely that this argument will be used in relation to other jurisdictions where there are delays in the court system.

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Contract

COURT OF APPEAL RULES ON PENALTY CLAUSES

Cavendish Square Holdings BV & anr v Makdessi [2013] EWCA Civ 1539, 26 November 2013

The Court of Appeal has reviewed the law on penalties and given an important decision on when a clause will be penal. The test for whether a clause is permitted is twofold: first, there must be a genuine pre-estimate of loss such that the clause is not extravagant and unreasonable; secondly, if there is no such estimate, there must be a commercial justification.

Background

The issue in this appeal was whether two clauses in an agreement for the sale of shares were unenforceable on the grounds that they were penalties.

Mr Makdessi was a key figure in the advertising and marketing world of the Middle East. He had founded a group which became the largest advertising and marketing communications group in that region.

By an agreement dated 28 February 2008 Mr Makdessi and a Mr Ghossoub agreed to sell to Young & Rubicam International Group BV 474 shares in Y&R Holdings Hong Kong Ltd, being 47.4% of its shares then in issue. Young & Rubicam International Group BV transferred its shares in Y&R Holdings Hong Kong Ltd to Cavendish Square Holdings BV and by a novation agreement of 29 February 2008 Cavendish Square Holdings B.V. was substituted for Young & Rubicam International Group BV as a party to the agreement. Cavendish is a sub-holding company within the WPP group. The result of the agreement was that Cavendish came to hold 60% of Y&R Holdings Hong Kong Ltd and Mr Makdessi and Mr Ghossoub retained 40%.

The consideration under the agreement included an earn-out element, referred to as an "Interim Payment" and a "Final Payment", in each case to be calculated by reference to future profits.

Clause 5.1 of the agreement provided that:

"*If a Seller becomes a Defaulting Shareholder he shall not be entitled to receive the Interim Payment and/or the Final Payment which would other than for his having become a Defaulting Shareholder have been paid to him and the Purchaser's obligations to make such payment shall cease*".

The definition of Defaulting Shareholder includes "*a Seller who is in breach of clause 11.2*". Clause 11.2 contained various restrictive covenants and was prefaced by clause 11.1 which provided that:

"*Each Seller recognises the importance of the Group to the Purchaser and the WPP Group which is reflected in the price to be paid by the purchaser for the Sale Shares. Accordingly, each Seller commits as set in this Clause 11 to ensure that the interest of each of the Purchaser and the WPP Group in that goodwill is properly protected.*"

Clause 5.6 (the **Call Option**) further provided that:

"*Each Seller hereby grants an option to the Purchaser pursuant to which, in the event that such Seller becomes a Defaulting Shareholder, the Purchaser may require such Seller to sell to the Purchaser (or its nominee) all (and not some only) of the Shares held by that Seller (the Defaulting Shareholder Shares). The Purchaser (or its nominee) shall buy and such Seller shall sell with full title guarantee the Defaulting Shareholder Shares… within 30 days of receipt by such Seller of a notice from the Purchaser exercising such option in consideration for the payment by the Purchaser to such Seller of the Defaulting Shareholder Option Price* [defined as *"an amount equal to the Net Asset Value* [NAV] *on the date that the relevant Seller becomes a Defaulting*

Shareholder multiplied by" the percentage which represents the proportion of the total shares the relevant Seller holds]."

The net effect of clauses 5.1 and 5.6 was that, if he breached his restrictive covenants, Mr Makdessi would lose his entitlement to his share of the Interim Payment and the Final Payment (which could have amounted to anything from zero to over USD 44 million, being the relevant cap, depending on future profits) and be liable to have his retained shares purchased under the Call Option (calculated by reference to net asset value, which would not take account of goodwill).

Mr Makdessi went on to breach the restrictive covenants in clause 11.2, as he later admitted (see the post-script below). The High Court had found the restrictive covenants to be valid and enforceable and there was no appeal from that decision.

Makdessi's case

Mr Makdessi argued that the doctrine of penalties applied to both clauses 5.1 and 5.6 and that they were penal. Clause 5.1, he argued, operated on breach since it took effect when a Seller became a Defaulting Shareholder which occurred, relevantly, on a breach of clause 11 and, if valid, disentitled him from receiving a sum which would otherwise be due to him. Clause 5.6 also, he said, operated on breach for the same reason.

Cavendish's case

Cavendish argued that these contentions rested on an erroneous basis. Although clauses 5.1 and 5.6 operated upon a breach of contract, they were not provisions which purported to provide compensation for breach. For provisions such as these, Cavendish submitted, the appropriate test was whether they have a commercial purpose and a commercial justification and lack a predominant intention to deter a breach (see "Commercial justification" below).

High Court (Mr Justice Burton)

Mr Justice Burton found at first instance that clauses 5.1 and 5.6 were not, on their own or together, penalties. There had been a commercial justification (the adjustment of consideration between the parties based on substantial loss of goodwill and the de-coupling of the parties on a speedy and conventional basis), the provisions were not extravagant or oppressive, the predominant purpose had not been to deter breach, and they had been negotiated on a level playing field.

A complicating factor, however, was that Mr Makdessi had previously made an offer to the company in respect of his breach of fiduciary duty as a director by virtue of his conduct which was also in breach of the restrictive covenants, in the sum of USD 500,000, and this had been accepted by the company. Mr Justice Burton considered this to be "double counting" which, he held, did render clause 5.1 a penalty. He therefore gave Cavendish the opportunity to repay this amount, as a term of the court making a declaration that it was not liable to make the Interim or Final Payment and ordering specific performance of the Call Option. In this respect, both sides contended that the judge was in error and the Court of Appeal agreed: the question of whether a clause is a penalty must be judged as at the date of the agreement in which it is contained, and cannot become so as a result of subsequent events.

Law on penalties

The Court of Appeal undertook an extensive review of the case law on penalties, which it acknowledged as a "*blatant interference with freedom of contract*". The older cases approached the issue of penalties on the footing of a dichotomy between a genuine pre-estimate of loss on the one hand and a penalty on the other. The modern authorities indicated that this was too rigid an approach. Recent cases showed the courts adopting a broader test of whether the clause was extravagant and unconscionable with a predominant function of deterrence and robustly declining to find that a clause was a penalty in circumstances where there was a commercial justification for that clause.

Genuine pre-estimate of loss

Against that background the Court of Appeal first considered whether clauses 5.1 and 5.6 were extravagant and unreasonable. It did not do so on the basis that the answer would be determinative as to whether the clauses were penal, but because the issue was undoubtedly a relevant one.

The Court of Appeal found that, when the agreement was entered into, Cavendish's damages for breach of the restrictive covenants were likely to be zero because they would be damages for loss of the value of its shareholding and thus reflective of a loss to the company itself. The Court of Appeal went on to say that, if the recoverable figure is zero, any estimate other than zero is excessive and a figure in the millions was on its face extravagant in comparison with the greatest loss.

At the time of the agreement, the sums that might be withheld from Mr Makdessi under clause 5.1 were undetermined but they could be anything from zero to over USD 44 million (the relevant cap for his potential share of the earn-out consideration), depending on the future profit calculation. The court was of the view that, whilst it was possible that a breach which caused Mr Makdessi to become a Defaulting Shareholder would so impact the goodwill of the company as to reduce the Interim and Final Payment to nothing, it considered that was a remote contingency against which it was likely, or at least readily foreseeable, that the sums forfeited would be millions or tens of millions of dollars. In the words of the court: "*The width of the* [restrictive] *covenants and the wide range of possible losses that might result from the operative breach are such that the amount likely to be withheld will in respect of part of the range be totally out of proportion.*" The Court of Appeal said that similar considerations applied in relation to the Call Option.

The Court of Appeal concluded that the clauses, taken in the context of the agreement as a whole, were not genuine pre-estimates of loss and were extravagant and unreasonable. The Court of Appeal said that was not, however, necessarily conclusive: a commercial justification may mean that a clause which is not a genuine pre-estimate is not penal.

Commercial justification

The Court of Appeal did not accept Cavendish's submissions that the provisions were commercially justified. In Cavendish's submission, the clauses were part of a commercial bargain, reached after extensive negotiation, as to the price payable for Mr Makdessi's shares. If Mr Makdessi did not abide by the restrictive covenants, which were there to protect the goodwill which underpinned a major part of the price, he would not receive the additional payments. In those circumstances, which would also indicate that it was no longer appropriate for him to remain a shareholder, he could also be required to sell his retained shares on a net asset value basis which did not reflect goodwill which he had shown himself unwilling to protect in the manner he had promised.

The Court of Appeal held that the underlying rationale of the doctrine of penalties was that the court will grant relief against the enforcement of provisions for payment (or the loss of rights or the compulsory transfer of property at nil or an undervalue) in the event of breach, where the amount to be paid or lost is out of all proportion to the loss attributable to the breach. If that is so, the provisions were likely to be regarded as penal because their function was to act as a deterrent. The examples from the cases of fulfilling some justifiable commercial or economic function included, held the court, a modest extra interest in respect of a defaulting loan; a provision for the payment of the costs of earlier litigation; a generous measure of damages for wrongful dismissal; an allocation of credit risk; or the provision of capital which would be needed if a promised guarantee of a loan was not forthcoming. Instead the effect in this case, the court held, was that Mr Makdessi stood likely to forfeit sums in the tens of millions in circumstances where, because of the unacceptability of double recovery, the law, for reasons of public policy, precludes any recovery by Cavendish at all. It was not sufficient, to describe, as Cavendish had, the clauses as having a commercial justification because they adjusted the consideration and effected a de-coupling. The important consideration was the terms on which the clauses provided for the price adjustment and de-coupling to take effect.

The Court of Appeal allowed the appeal, whilst ordering Mr Makdessi to repay the sum of USD 500,000 which had previously been agreed in settlement of the company's claim for breach of his fiduciary duty as a director.

COMMENT

Having decided that the relevant provisions should be interpreted as providing compensation for breach, the

thing that seemed most to trouble the court was that, in circumstances where there were a range of possible losses, the financial consequences under the agreement were the same. Moreover, the Court of Appeal was of the view that the financial consequences would, in respect of at least part of the range, be excessive and out of all proportion.

It seems from the dicta of the Court of Appeal that making payment conditional upon compliance, as opposed to withholding payment in the event of breach, may side step the law on penalties and that this is just one of the anomalies of the law in this area.

Either way, what is clear is that the court will subject these types of clauses to detailed scrutiny and the Court of Appeal's decision may signal a greater emphasis on there being a genuine pre-estimate of loss over commercial justification than some of the more recent authorities might be taken to suggest.

Post-script

The High Court had also granted Cavendish permission to apply to commit Mr Makdessi for contempt on the ground that he had made false statements in a document verified by a statement of truth concerning his actions as they related to his compliance with the restrictive covenants. Mr Makdessi also appealed this decision but this appeal was dismissed by the Court of Appeal.

An application for permission to appeal to the Supreme Court was filed by Cavendish on 20 December 2013.

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Costs

COURT OF APPEAL CONSIDERS "ECONOMIC REALITIES" IN AWARDING COSTS ORDER AGAINST A COMPANY DIRECTOR

Axel Threlfall v ECD Insight Ltd & anr [2013] EWCA Civ 1444, 29 October 2013

The Court of Appeal, in overturning an earlier High Court decision, has ruled that costs akin to those awarded against non-parties may in fact be awarded against a party to a claim. This is the first time the courts have exercised their discretionary powers relating to costs under s51 of the Senior Courts Act (the **SCA**) in this way. The court acted to ensure that after the defendant company had gone into liquidation, it was able to award a costs order against the company's sole director and shareholder (and co-defendant to the claim). The High Court had sought to establish the director's substantive liability before awarding costs, but this was held to be unnecessary. Rather the crucial considerations were the "economic realities" of the case and the director's poor conduct.

Background

Mr Threlfall was an employee of ECD. He brought an action for breach of his employment contract against ECD and its sole director and shareholder, Mr Whitney.
Mr Threlfall said that his employment contract was varied by agreement between himself and Mr Whitney and that he was therefore entitled to a 20% share in the equity of ECD, share dividends, a termination payment and a bonus payment. ECD denied the claim and counter-claimed, alleging breaches by Mr Threlfall both of his obligations of fidelity and also of restrictive covenants in his employment contract. Mr Whitney had been joined as a party to the action because any order for

specific performance (to procure the transfer or issue of shares to Mr Threlfall) would have required a transfer of shares by Mr Whitney or required ECD to issue and allot, therefore diluting Mr Whitney's sole shareholding.

The High Court decision

The High Court did not find Mr Whitney's evidence credible and further found that he "*was seeking to resile from the agreement he made … because the financial implications of doing so were damaging both to ECD and to himself personally*". Mr Threlfall was ultimately successful overall and judgment for Mr Threlfall was entered against ECD for the sums of money specified in the order (Mr Threlfall having elected to take payment rather than shares *in specie*). Judgment for ECD was entered against Mr Threlfall for nominal damages for breach of the obligation of fidelity.

Mr Threlfall's counsel applied to the judge that Mr Whitney should be jointly and severally liable with ECD for the costs of the action. It was submitted that this was the kind of case in which any application against Mr Whitney "*ought to be considered by analogy to a non-party costs order*" under s51 of the SCA).

Section 51(3) of the SCA states that "*the court shall have full power to determine by whom and to what extent the costs are to be paid*". The Court of Appeal had previously laid down guidelines for the exercise of this power against non-parties in *Symphony Group v Hodgson* [1993] 4 All ER 143, CA, including that such an order should always be exceptional.

The High Court said that ECD was a solvent company which ran a legitimate defence at trial and that it was not necessary for an order to be made against Mr Whitney. Less than a month later, ECD went into insolvent liquidation. Mr Threlfall appealed on the issue of the judge's order for costs only.

The Court of Appeal decision

Lewison LJ held that the High Court had erroneously linked the question of whether costs were payable by Mr Whitney to the question of Mr Whitney's own substantive liability in respect of the claim, with a positive finding as to the latter being held as a pre-condition to the former. It had therefore omitted to deal with the important point that non-party costs orders are made against persons against whom there is no substantive cause of action. Lewison LJ held that "*the exercise of discretion to make a non-party costs order leaves rights and obligations where they are*". This meant that there was no need to consider issues of piercing/lifting the corporate veil: the court was not fettered by legal realities and was entitled to look at economic realities. Accordingly, Lewison LJ listed eleven factors which he said, taken cumulatively, made it just for the court to allow the appeal and order costs against Mr Whitney. These factors included: that the High Court stated that ECD was under Mr Whitney's absolute control, he did not regard himself as accountable to anyone else, Mr Whitney sought to resile from the contract and Mr Whitney's evidence was given in bad faith.

COMMENT

This case evidences the wide-ranging discretion the courts have under s51 of the SCA in determining costs orders, with the Court of Appeal ruling for the first time that in certain circumstances it might be appropriate to impose what is essentially a non-party costs order on a party to a claim. It confirms that the court will look first and foremost at achieving a just outcome for the parties, taking into account factors such as the economic realities of the case and the conduct of the parties involved.

Further, the court's confirmation that, in exceptional circumstances, a costs order analogous to a non-party costs order could be made against a director of a company without piercing the corporate veil (as the question of his own substantive liability was irrelevant for the purposes of the order) is of particular note.

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Damages

THE COMMERCIAL COURT CONSIDERS THE DATE AT WHICH LOSS SHOULD BE ASSESSED WHERE DAMAGES ARE SOUGHT AS A RESULT OF ALLEGED NEGLIGENT FINANCIAL ADVICE

Gestmin SGPS SA v Credit Suisse (UK) Ltd & anr [2013] EWHC 3560 (Comm), 15 November 2013

The Commercial Court has held *obiter* that losses resulting from alleged negligent financial advice should be assessed as at the date of the trial. In reaching this decision, the Commercial Court held *obiter* that the general rule in contract and tort that damages should be assessed as at the date of the breach in question did not apply in this case.

Background

In 2005, the claimant entered into an agreement with the defendants under which the defendants agreed to provide private banking services to the claimant, including general investment advisory and dealing services in securities (the **Agreement**).

After entering into the Agreement, the claimant made a series of investments in financial products based on advice provided by the defendants. One of the investments was in the shares of a company, QWIL. However, during the sub-prime mortgage crisis the value of the QWIL shares decreased significantly.

In 2006, the claimant sold a small number of its QWIL shares but was unwilling to sell any further QWIL shares at the prices offered in the market which were substantially lower than the price it had originally paid for the QWIL shares.

In 2007, QWIL made two tender offers to purchase a certain number of its own shares at a price which was substantially lower than the price that the claimant had originally paid for the QWIL shares. The claimant chose not to participate in these tender offers.

The claim

The claimant alleged that the defendants' investment advice in relation to the QWIL shares had been negligent on the basis that:

- the QWIL shares were an unsuitable investment for the claimant because it was an investment with high risk and low liquidity; and
- the defendants misrepresented or failed to properly explain the risks of investing in the QWIL shares.

In particular, the claimant argued that that the defendants owed it a duty of care to explain and ensure that it understood the nature and risks of proposed investments. In support of this argument, the claimant referred to Rule 5.4.3 of the FSA's Conduct of Business Rules (the **COBs**) which provided that a firm must not make a personal recommendation of a transaction to a private customer "*unless it has taken reasonable steps to ensure that the private customer understands the nature of the risks involved*".

The claimant brought proceedings against the defendants and sought damages for the losses it alleged that it had suffered as a result of having invested in the QWIL shares.

Judgment

The Commercial Court found that the claimant had failed to establish that the defendants had breached their contractual and tortious duties towards it. As a result, it was held that the defendants had no liability to the claimant.

Leggatt J found that Rule 5.4.3 of the COBs did not apply as the claimant did not fall within the definition of a "private customer" for the purposes of the COBs as it was a body corporate with net assets of at least GBP 5 million and was not a market counterparty for the purposes of the COBs.

Although Leggatt J confirmed that the defendants' duties towards the claimant may be informed by relevant regulatory rules, he rejected the claimant's "*unqualified assertion*" that investment advisors had a duty to ensure that its client made informed investment decisions:

"*It seems to me that the extent of an advisor's responsibility to explain the nature and risks of a transaction must depend on the particular circumstances. I would accept, however, that where an advisor recommends an investment by pointing out potential benefits to the client, the advisor must take care to ensure that the presentation is a fair one and that it is not skewed or misleading by reason of omitting to mention material risks. What risks are sufficiently material that they ought to be specifically explained or highlighted is a matter of fact which depends on the context*" (paragraph 124).

Leggatt J's decision in this respect was consistent with established legal principles, including the Court of Appeal's recent decision in *Green and Rowley v The Royal Bank of Scotland plc* [2013] EWCA Civ 1197 which was handed down during this trial (and covered in the November/December 2013 Litigation Review).

Obiter comments regarding quantum

Notwithstanding the overall decision in this case, Leggatt J still continued to consider on an *obiter* basis the date at which the claimant's losses would have been assessed in the event that the claimant's claim had been successful.

Leggatt J started by considering the general rule in contract and tort that damages are to be assessed as at the date of breach. However, Leggatt J also noted that damages may be assessed by reference to an alternative date "*if the court considers that to do so would more fairly and appropriately give effect to the basic compensatory principle of seeking to put the claimant in the same financial position as if the wrong had not occurred*".

According to the principles set out in *Smith New Court Securities Ltd v Scrimgeour Vickers (Asset Management) Ltd* [1997] AC 254, Leggatt J found that the appropriate date at which to assess the claimant's loss will generally be the earliest date at which:

- the claimant was aware of the facts giving rise to the claim;
- the claimant could have readily sold the assets purchased as a result of the defendant's wrongdoing at a price which fairly reflected the value of the assets; and
- it would not have been unreasonable for the claimant to sell the assets.

Based on these principles, Leggatt J found that the claimant may have been able to sell more of its QWIL shares than it did, and could probably have sold its entire shareholding over time if it had been willing to accept lower prices for the shares. However, Leggatt J also found that the evidence as a whole indicated that the claimant could not have sold its QWIL shares "*other than with difficulty and a significant loss of value*". As a result, Leggatt J held *obiter* that had the claimant's claim been successful he would have assessed the claimant's loss as at the time of the trial and not as at the time of the alleged breach (as the defendants had argued).

Witness testimony

Leggatt J made some interesting observations about witness recollection and testimony concluding that "*the best approach for a judge to adopt in the trial of a commercial case is, in my view, to place little if any weight at all on witnesses' recollections of what was said in meetings and conversations, and to base factual findings on inferences drawn from the documentary evidence and known or probable facts*….".

COMMENT

Leggatt J's *obiter* comments regarding the date at which the claimant's losses would have been assessed are consistent with the Court of Appeal's decision in *Hooper & anr v Oates* [2013] EWCA Civ 91 which surprisingly was not referred to in his judgment.

Nonetheless, this case provides a helpful insight as to how the issue of the time at which a claimant's losses should be assessed will be considered in cases concerning alleged negligent financial or investment advice.

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Regulatory

WARNING NOTICES AND PRIVILEGE ISSUES

Ford, R (on the application of) v The Financial Services Authority [2013] EWCA Civ 1521, 19 July 2013

The Court of Appeal considered whether there was a real prospect of success of an appeal against a refusal of the High Court to quash warning notices issued by the Financial Services Authority (**FSA**) (now the Financial Conduct Authority (**FCA**)) against the applicant, Mr Ford. The appeal was also brought against the High Court's decision not to order the removal from the continuing investigation of the FSA officials who had seen emails which the High Court had held to be subject to legal professional privilege.

The case arose out of an investigation by the FSA into Key Data Investment Services Ltd (**Key Data**) which commenced in December 2007 and an investigation into three Key Data executives, including Mr Ford in his capacity as Director and Chief Executive Officer of Key Data. In 2011 the applicant was successful in arguing in a claim for judicial review that two of the emails obtained during the course of these investigations should not have been relied on by the FSA as they attracted joint interest privilege and the executives had not waived privilege. However, in the exercise of its discretion, the High Court had refused to quash the notices in question.

The Court of Appeal dismissed Mr Ford's application for leave to appeal. In doing so it confirmed that the High Court, notwithstanding that a breach of the applicant's rights under Article 8 of the European Convention on Human Rights (**ECHR**) had occurred in this case, always retained a discretion as to the remedy to be granted. The Court of Appeal saw no reason to interfere with the view taken by the High Court that the reliance by the FSA on the privileged material in question was, in essence, peripheral and would not have made a material difference to the outcome of their decision to issue the notices in question. The Court concluded that the applicant had not satisfied the Court that he had a real prospect of showing that the judgment of the lower court was wrong.

The facts

The claimant, Mr Ford, was a former Director and Chief Executive Officer of Key Data. He was also the

majority shareholder of that company. Key Data was regulated by the FSA. In January 2008 a law firm, Irwin Mitchell, was retained by Key Data in relation to an investigation launched by the FSA in December 2007 into the actions of Key Data in respect of the marketing and selling of a particular financial product. The engagement letter in January 2008 made it clear that the services of the law firm were engaged only to provide advice to Key Data while noting that there was a risk that the investigation may widen into the activities of individual directors. Advice contained in eight emails was sent between February and June 2008 by the solicitor concerned to the executives at their work emails. In September 2008 the FSA notified three executives of Key Data, including the applicant, that they too were being investigated. In June 2009 Key Data went into administration and Irwin Mitchell ceased to act for Key Data. From that point on, the applicant sought independent advice from other solicitors. In August 2009 the FSA compelled the administrators of Key Data to disclose the executives' email correspondence which included correspondence with Irwin Mitchell. The applicant sought unsuccessfully to prevent the Regulatory Decisions Committee from viewing the emails in question when it reached its decision to issue warning notices against the claimant and the other two executives in October 2010.

In 2011 the applicant successfully argued in a claim for judicial review that two of the emails between the law firm and Key Data executives could not be relied on by the FSA as they attracted joint interest privilege and the executives had not waived privilege.

However, the court, when considering which remedies to grant, found that the legally professionally privileged material formed only a very small part of the detailed material on which the FSA relied in the warning notice. The judge held that it was difficult to see that the warning notice would not have been issued if the FSA had not had the legally professionally privileged material. He held that the applicant would be sufficiently protected if the warning notice was redacted. The judge was assured that no member of the Regulatory Decisions Committee who had decided to issue the warning notice would have any further involvement in the process and held that it was not necessary to make an order in that regard. Mr Ford had been seeking an order that the officials previously involved in the investigation who had seen the material in question should no longer be involved.

Grounds of appeal and decision of the Court of Appeal

The two main grounds of appeal advanced against the decision not to quash the warning notices were that (a) the warning notices should have been quashed on the ground that the rules of natural justice had been breached in that Mr Ford had had no proper opportunity to comment on the material in the warning notices due to the reference in those notices to legally privileged material and (b) the High Court did not have discretion to refuse to quash the warning notices.

The Court of Appeal dismissed the first ground out of hand, noting that since these were "minded to" notices, the applicant still retained an opportunity to comment on the contents of the notices.

In respect of the second ground, the court considered the breach of a limited Convention right by the FSA (in this case the interference with Mr Ford's right to respect for private life under Article 8) meant that the court always had a discretion when considering how to remedy the violation of that right and that the court "*must … act in a way which is just and which is proportionate having regard to all the circumstances ….*". It saw no reason to interfere with the assessment of the court below that ultimately the erroneous reliance on the legally privileged material would not have made a material difference to the decision to issue the notices.

The court also refused to interfere with the finding of the High Court's evaluation that the continued involvement of the officials in question would cause no real prejudice to Mr Ford.

COMMENT

This case should serve as a reminder that even if legally privileged material has been erroneously relied upon by a regulator, the court will always assess whether the material made a difference to the outcome of the decision in question.

The Court of Appeal acknowledged in its judgment that there is balance that needs to be struck even at the preliminary stage of an investigation between the need for regulatory bodies to be able to investigate and to make preliminary findings and the fairness to an individual who may, particularly in a complex process, find that the process takes a long time. The proportionality and transparency of regulatory investigations particularly at an early stage of an investigation is a controversial issue: as the court noted, issues of fairness and due process at this stage of investigation been the subject of a number of cases. The FCA has a wide range of enforcement powers including the power to publish warning notices about firms and individuals which are intended to encourage more compliant behaviour. Last autumn the FCA issued a policy statement on publishing information about enforcement warning notices proposing that information would be published along with warning notices. This is a new development to the warning notice regime which will no doubt create further controversy and possible legal challenges by recipients of such notices.

WHERE ON THE WEB

http://www.fca.org.uk/static/documents/policy-statements/ps13-9.pdf

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BANKING REFORM ACT: ISSUES FOR LITIGATORS

The Financial Services (Banking Reform) Act 2013 (the **Act**) received Royal Assent on 18 December 2013 and the Government announced that it was "the biggest reform to the UK banking sector in a generation". Much has been written about the introduction of the ringfence that will separate retail banking from investment banking, the bail-in tool and the creation of a new regulator for the payments system, but what does the Act mean for litigators and those with a contentious regulatory practice?

New regime for senior managers

Banking Standards (**PCBS**) recommended a new senior persons regime to replace the Significant Influence Function element of the Approved Persons Regime.
The PCBS identified two key purposes for creating the new regime: first, to encourage greater clarity of responsibilities and improved corporate governance within banks; and, secondly, to establish beyond doubt individual responsibility in order to provide a sound basis for the regulators to impose remedial requirements or to take enforcement action where serious problems occur.

Key features of the new regime

The senior managers regime will apply to UK banks, building societies, credit unions and PRA-regulated investment firms who have permission to deal as principal.

Reverse burden of proof

The reversal of the burden of proof, as set out in the new ss66A(6) and 66B(6) of the Financial Services and Markets Act 2000 (**FSMA**), is one of the more controversial provisions in the Act. The new provision provides that a person who was a senior manager in relation to a relevant authorised person at the time of the contravention occurring or continuing, and was responsible for the management of any of the authorised person's activities in relation to the contravention, is not guilty of misconduct if he satisfies the Financial Conduct Authority (**FCA**) or Prudential Regulation Authority (**PRA**) that he has taken such steps as a person in his position could reasonably have been expected to take to avoid the contravention occurring or continuing. As such it is for the person

accused of misconduct to prove that he is not guilty of misconduct; the burden of proof is not on the FCA or PRA. This could lead to the FCA commencing significantly more cases against senior managers given that this reversal could potentially mean that much less of the FCA's resource will be required at the outset of the investigation.

Additional responsibility on senior managers

There will be mandatory statements of responsibility for senior managers to specify more clearly the areas of the business they have oversight of. This will assist the FCA in identifying to a greater extent the individual(s) with responsibility for the relevant parts of a firm where failings have been identified. There will also be provision for time-limited/conditional approvals of senior bankers, and regulators will be able to make conduct rules for senior managers.

Not just senior managers

A significant change under the Act is to expand the FCA's remit beyond approved persons to include *employees* of "relevant authorised persons". A "relevant authorised person" is defined as a deposit-taking institution, or an investment firm which deals in investments as principal and carries out activity regulated by the PRA. This is a fundamental change to the existing regime and could lead to enforcement action against a much larger group of individuals. The FCA has stated that it intends to issue a consultation on the scope of this change and the senior managers regime later this year.

Limitation period extended

Another key change is the extension of the limitation period from three years to six years during which the FCA or PRA can impose a penalty on someone who has performed a controlled function without approval.

New criminal offence

During a House of Commons debate on 11 December 2013, the Financial Secretary to the Treasury set out the rationale behind introducing a new criminal offence relating to a decision which causes a UK financial institution to fail.

He said: "*The introduction of this offence means that … those who bring down their bank by making thoroughly unreasonable decisions can be held accountable for their actions. In line with the commission's recommendations, the new offence will be applicable only to individuals who are covered by the senior managers regime. The maximum sentence for the new offence will be seven years in prison and/or an unlimited fine. That reflects the seriousness that the Government and society more broadly, places on ensuring that our financial institutions are managed in a way that does not recklessly endanger the economy or the public purse*".

The offence

A person commits an offence if, at a time when he is a senior manager in relation to a UK financial institution (broadly banks and building societies, but not insurers or credit unions):

- he takes (or agrees to the taking of) a decision by or on behalf of that financial institution as to the way in which it (or a member within its group) conducts business or fails to take such steps as he could have done to prevent that decision being taken;
- he is aware, at the time the decision is made, of a risk that the implementation of the decision may cause the financial institution (or a member of its group) to fail;
- he behaves, in all the circumstances, in a way that falls far below what could reasonably be expected of a person in his position in relation to the taking of the decision; and
- the implementation of the decision causes the failure of the financial institution (or that of a member of its group).

Note that the offence requires actual knowledge of the risk – it will not be sufficient that the manager in question ought to have known of such a risk.

The penalty

Nevertheless, the stakes are high. A person convicted of this offence is liable:

- on summary conviction (in England and Wales), to imprisonment for a term not exceeding 12 months (or six months if the offence was committed before the commencement of s154(1) of the Criminal Justice Act 2003), or a fine, or both; and

– on indictment, to imprisonment for a term not exceeding seven years, or a fine, or both.

COMMENT

The changes summarised above will have a fundamental impact on senior managers and on a much wider group of employees who have previously not fallen under the scrutiny of the regulator.

The new regime for senior managers and the new criminal offence are expected to be implemented in mid-2015. The FCA and PRA will refine how the senior managers regime will take shape throughout the course of this year. Although we await the details of these, enforcement cases are likely to be brought against individuals more frequently and with a higher success rate.

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Top banking litigation and regulatory decisions from 2013

Set out below is a summary of the most interesting banking litigation and regulatory decisions from 2013. The selection is necessarily subjective and draws from a wide range of cases reported in the 2013 Allen & Overy Litigation Reviews which are of direct relevance to finance parties.

LIBOR test cases

Deutsche Bank & ors v Unitech Global Ltd & anr [2013] EWCA Civ 1372

The Court of Appeal found that, by proposing LIBOR as a reference rate in a contract, it was at least arguable that two LIBOR panel banks impliedly represented that their LIBOR submissions were honest. The court considered that an allegation of an implied representation was fact-specific so it would be dangerous to dismiss it summarily rather than allowing it to be considered at trial. The finding may open the door for further claims by counterparties to contracts with LIBOR panel banks. The Court of Appeal's decision is the first decision of an appellate court to consider in what circumstances a party can allege that implied representations as to LIBOR have been made. Allen & Overy LLP represented the Lenders as respondents to the appeal brought in Claim No 2011 Folio 1199. The appeal in the Unitech proceedings was conjoined with an appeal of an earlier decision of Mr Justice Flaux in *Graiseley Properties Ltd & Ors v Barclays Bank Plc*. Permission to appeal to the Supreme Court has been filed.

Scope of bank's duties

Agent bank

Torre Asset Funding Ltd & anr v Royal Bank of Scotland plc [2013] EWHC 2670, 3 September 2013

Sales J considered the role of an agent bank under standard contractual provisions in a structured financing and found that the ambit of the role was defined purely in the transaction documents. The bank successfully defended claims brought by disgruntled junior mezzanine lenders after the borrower became insolvent. The court held that a contractual provision that

described the agent's duties as "*solely mechanical and administrative in nature*" must be read subject to specific provisions in the relevant agreements which imposed duties or conferred discretions on the agent. The role of agent, while not purely a "*postal service*", is, however, limited in nature and is not intended to include having to undertake an evaluative analysis of whether an Event of Default has occurred. The judge also found, however, that the bank had assumed a responsibility for the accuracy of the explanation it offered in respect of a request for consent to the "rolling-up" of interest. Although the bank had (albeit not deliberately) breached its duty, the breach had not caused the defendant any loss. Subject to appeal.

Securities lending agent

AP-Fonden v Bank of New York Mellon SA/NV & ors [2013] EWHC 3127 (Comm), 16 October 2013

In a negligence claim for damages arising out of a failed investment, the High Court considered the role of a securities lending agent that had been appointed to invest and manage its client's cash collateral reinvestment portfolio. This case reiterates the nature and extent of a lending agent's duty of care within the confines of a non-fiduciary agent/client relationship.

Sale of interest rate swaps

John Green & anr v Royal Bank of Scotland plc [2013] EWCA Civ 1197, 9 October 2013

The Court of Appeal dismissed an appeal brought by two individuals (the Appellants) in relation to alleged mis-selling of an interest rate swap by the Royal Bank of Scotland. The decision is favourable for financial institutions that are the subject of pending claims regarding the sale of interest rate swaps. This is because Tomlinson LJ was very clear that claimants should not be able to import the duties owed by financial institutions under the FCA's Conduct of Business Rules (**COB Rules**) into the common law, which would make them available to a broader category of persons than is currently the case under s150 (now s138D) Financial Services Markets Act 1986. However, this case is highly specific to its own facts. Furthermore, the fact that the Appellants had conceded, before their case reached the Court of Appeal, that their claim against the Bank for a breach of its statutory duties under the COB Rules pursuant to s150 FSMA was time-barred meant that the appeal got off to what Tomlinson LJ described in his judgment as "*a distinctly unpromising start*". It therefore remains to be seen what approach the courts will take to interest rate swap mis-selling claims which concern alleged breaches of statutory duties and are not time-barred.

Application of COB suitability requirements

Zaki & ors v Credit Suisse (UK) Ltd [2013] EWCA Civ 14

The Court of Appeal upheld a High Court ruling that the sale of structured notes to a high net worth individual was suitable notwithstanding the high degree of leverage involved. In doing so, it considered how the suitability requirements under the COB Rules and their successor (the Conduct of Business Sourcebook Rules (COBS)) apply to the issue of leverage in investments where advice has been provided.

Contract

A common sense approach to "business common sense: Rainy Sky refined"

BMA Special Opportunity Hub Fund Ltd & ors v African Minerals Finance Ltd [2013] EWCA Civ 416, 23 April 2013

The Court of Appeal confirmed that the "business common sense" approach to contractual interpretation expounded by the Supreme Court in *Rainy Sky v Kookmin* [2011] 1 WLR 2900 is neither an overriding principle of construction nor a licence for one party to say that a contract means what amounts to "good business sense" to that party.

Interpretation of Material Adverse Change clause

Grupo Hotelero Urvasco SA v Carey Value Added SL (formerly Losan Hotels World Value Added I SL) & anr [2013] EWHC 1039 (Comm), 26 April 2013

Material Adverse Change clauses are common in credit agreements but are rarely interpreted by the courts. In this case Blair J considered what can be taken into account when considering a borrower's "financial condition", how to assess the "materiality" of any change in financial condition and to what extent a lender's knowledge of pre-existing financial

circumstances at the time of granting credit can be considered when assessing whether a material change has occurred.

English Court upholds hybrid justice clause

Mauritius Commercial Bank Ltd v Hestia Holdings Ltd & Sujana Universal Industries [2013] EWHC 1328 (Comm)

Popplewell J held that the parties to a loan agreement were able to amend the governing law of an asymmetric jurisdiction clause from Mauritian to English law. Popplewell J also robustly confirmed the enforceability of asymmetric jurisdiction clauses as a matter of English common law. In doing so, he commented on the controversial decision on the enforceability of such clauses as a matter of EU law handed down by the French Cour de cassationin 2012 in *Banque Privee Edmond de Rothschild Europe v X*. The decision is a helpful one for parties seeking to rely on such clauses in future.

Doubt over the effectiveness of anti-discharge provisions

CIMC Raffles Offshore (Singapore) Ltd & anr v Schahin Holdings SA [2013] EWCA Civ 644, 7 June 2013

The Court of Appeal allowed an appeal in a case concerning the extent to which a guarantee still applies if the guaranteed contract has been varied so that it fundamentally differs from the original guaranteed contract which was entered into by parties. The Court of Appeal considered the purview doctrine and whether it could be excluded by the inclusion of anti-discharge or anti-avoidance wording in guarantees. The Court of Appeal concluded that the purview doctrine was unclear and that anti-discharge or anti-avoidance provisions in guarantees may not always have the effect of excluding the effect of the "purview" doctrine. It added that there was no previous authority on this, and there was at least an arguable case that such provisions would not exclude the purview doctrine.

Regulatory

No judicial review of FSA decision notice

R (on the application of Christopher Willford) v Financial Services Authority [2013] All ER (D) 114

Having regard to the principle that, save in exceptional circumstances, proceedings for judicial review cannot be brought where there is an alternative remedy available, the Court of Appeal rejected a claim for judicial review by a finance director who sought to quash, for lack of proper reasons, a decision notice issued by the Financial Services Authority.

Court of Appeal dismisses appeal against finding of market abuse by the Upper Tribunal

(1) 7722656 Canada Inc (formerly carrying on business as Swift Trade Inc), (2) Peter Beck v The Financial Conduct Authority [2013] EWCA Civ 1662

A defunct day-trading company controlled by a prominent Canadian entrepreneur was ordered to pay an GBP 8 million fine for market abuse for moving share prices on the London Stock Exchange through rapidly placing and cancelling orders from all over the world on thinly traded companies. The ruling penalises the company for "layering" – market slang for using multiple orders to move share prices in a particular direction.

Restructuring

Supreme Court considers the tests for insolvency

BNY Corporate Trustee Services Ltd v Eurosail-UK 2007-3BL plc [2013] UKSC 28

The Supreme Court ruled on the construction and effect of the "balance-sheet" insolvency test (s123(2) Insolvency Act 1986) and its interaction with the "cash flow" insolvency test (s123(1)(e)). The decision is relevant not just to winding-up petitions but also to insolvency related events of default that are commonly incorporated in finance documents.

Consent payments to noteholders allowed

Sergio Barreiros Azevedo & anr v Imcopa Impotaçoa, Exportação e Indústria de Olèos LTDA [2013] EWCA Civ 364, 22 April 2013

The Court of Appeal upheld a decision that it is not unlawful under English law for an issuer to offer a "consent payment" to noteholders who vote in favour of a resolution proposed for their consideration as a class. The issuer in this case had solicited and procured votes in support of a financial restructuring proposal by offering and making cash payments to those members

of the relevant class (noteholders) who voted in favour of the proposal but excluded from the payment those who voted against it or who did not vote at all. Another case from 2012 (*Assenagon Asset Management SA v Irish Bank Resolution Corp Ltd* [2012] EWHC 2090 (Ch)) showed that not all incentives for noteholders will be allowed by the courts. In that case Briggs J held that a process whereby bondholders had been asked to vote in favour of a proposal which involved the exchange of their bonds for the issue of new bonds, had not been undertaken validly.

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