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Review

EDITORIAL

Cross-border transaction certainty requires the parties' choice of governing law to be upheld. The prospect that mandatory local laws might be applied by a court notwithstanding the express choice of another governing law is one of the threats to legal certainty. In the derivatives context, there has been an important Court of Appeal ruling denying the application of mandatory rules of Italian financial services law to swaps between an Italian local authority and a bank. Allen & Overy acted for the successful appellant bank. We also cover another decision in the Italian local authority/swaps context, this time on competing jurisdiction clauses.

Cross-border transactions can of course lead to cross-border litigation, which is when certain boilerplate clauses can suddenly be under the spotlight. How can a foreign party be served if, for example, its appointment of an agent for service of process has lapsed? Can a foreign counterparty be served by the claimant serving a claim form on an agent in the UK? These are the subjects of two rulings covered in this edition.

We also discuss a case considering whether certain clauses should be construed '*contra proferentem*' – ie against the party seeking to rely on the clause. The Court of Appeal's decision confirms the limited application of this rule in relation to commercial contracts.

Legal privilege remains a hot topic for discussion. After last month's storm following the ruling on litigation privilege in investigations in the ENRC/SFO case, another privilege ruling (this time on without prejudice privilege) has considered the application of exceptions to the without prejudice rule where disclosure to a third party is contemplated. Our article draws out the practical implications, in terms of potential disclosure to a third party, for parties negotiating on a without prejudice basis.

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Conflict of laws

MANDATORY RULES OF LOCAL LAW DO NOT APPLY TO INTEREST RATE SWAPS BETWEEN A BANK AND AN ITALIAN LOCAL AUTHORITY

Dexia Crediop S.p.A. v Comune di Prato [2017] EWCA Civ 428, 15 June 2017

The Court of Appeal has overturned a decision of the High Court that an Italian local authority could rely on local mandatory laws to invalidate an interest rate swap entered into with an Italian bank. In its ruling the Court emphasised that swaps entered into on ISDA form documentation, where there are related back-to-back hedging transactions, form part of a market which is inherently international. This is a significant ruling for many other similar disputes involving local authorities and financial institutions. Following the approach in its decision in *Banco Santander Totta SA v Companhia Carris De Ferro De Lisboa SA & ors* [2016] EWCA Civ 1267, the Court of Appeal has endorsed the view that Article 3(3) of the Rome Convention (**Article 3(3)**) is to be approached as a limited exception to the principle of party autonomy to choose the governing law. Accordingly, the Court of Appeal's approach to the scope of Article 3(3) will be of interest to parties concerned about the potential for mandatory rules of local law to undermine the parties' choice of law.

Background

Between 2002 and 2006, Dexia and Prato entered into a number of interest rate swaps. This included an interest rate collar swap entered into in 2006 (the **Swap**). Under the Swap, Prato agreed to pay an interest rate no higher than the cap rate but no lower than the floor rate. In return it would receive EURIBOR. The Swap comprised a 1992 Multi-Currency Cross-Border form ISDA Master Agreement and confirmations incorporating an express choice of English law and jurisdiction.

All proceeded smoothly until the financial crisis and the subsequent fall in interest rates to historic lows. This meant that the floor rate payable by Prato under the swap exceeded the prevailing floating rates which it was receiving. In 2010, Prato took steps in Italy to set aside the Swap. In response Dexia brought a claim in the English Commercial Court for payment and declaratory relief as to the validity of the Swap (and prior swaps). Prato's defence and counterclaim was based primarily on Italian law arguments relating to its: (i) capacity to enter in to the Swap; and (ii) mandatory provisions of Italian financial services law, which Prato argued applied by virtue of Article 3(3) of the Rome Convention (**Article 3(3)**), both of which rendered the swaps invalid or unenforceable.

Swaps declared null and void at first instance

While Dexia defeated most of the major defences raised, the High Court held that Article 3(3) was engaged. As a result of breaches of the applicable mandatory rules of Italian financial services law, notably those related to offsite sales and distance marketing, the Swap was declared null and void. Dexia appealed.

Article 3(3) did not apply to the swaps

Article 3(3) provides that the choice of English law as the governing law of a contract shall not prejudice the application of the "mandatory rules" of the law of the one country with which "all the other elements relevant to the situation at the time of the choice are connected".

The Court of Appeal upheld Dexia's appeal, and ruled that Article 3(3) did not apply to the swaps.

The Court of Appeal followed the approach in its decision in *Banco Santander Totta SA v Companhia Carris De Ferro De Lisboa SA & ors* [2016] EWCA Civ 1267 and asked whether, other than the English

governing law and jurisdiction clause, "all other elements relevant to the situation are connected with one country only" (ie Italy). In doing so, the Court confirmed that the Judge at first instance had erred when he based his evaluation on the identification of elements connected to another country other than Italy in a conflict of laws sense. Instead, the Court of Appeal confirmed again that the correct approach is to establish whether there is an "international and relevant element in the situation" which makes it impossible to say that all "all elements (other than the choice of law) relevant to the situation are located in a country other than England".

"Elements relevant to the situation"

In its re-evaluation of the "elements relevant to the situation", the Court of Appeal held that the following were important factors:

- The choice of ISDA documentation, which was itself an international element rather than a domestic element associated with any particular country.
- The Multi-Currency – Cross Border form contemplates more than one currency and the involvement of more than one country, and the ISDA Master Agreement was in English despite that not being the first language of either party.
- The back-to-back swaps entered into by Dexia were routine and "the fact that they were made with banks outside Italy shows just how international the swaps market actually is".

ISDA Master Agreement operates in an international market

The Court of Appeal expressly recognised that the ISDA Master Agreement is used precisely because it is not intended to be associated exclusively with any one country and forms part of an international swaps market. For the Court of Appeal, the presence of back-to-back hedging contracts was "highly significant" and supports the need for certainty in the scope of application of mandatory local rules in an international market. As noted by the Court of Appeal, if mandatory local laws of a party are to be applied to an individual swap contract in isolation, there is a "real risk that the back-to-back security will quickly become illusory". The Court of Appeal has therefore endorsed the view that Article 3(3) is to be approached as a limited exception to the principle of party autonomy to choose governing law.

***Obiter* – application of Italian financial services law**

While the Court of Appeal's decision on Article 3(3) meant that the Italian mandatory law defences did not apply, the Court went on to overturn two out of three of the Judge's findings on alleged breaches of Italian financial services law related to distance marketing and requirements relating to the form of the contract. The Court of Appeal upheld the Judge's finding in respect of Article 30 of the Testo Unico della Finanza (**TUF**) in force at the time and held that as a matter of Italian law a bank is required to include a seven-day right of withdrawal in investment contracts with retail investors entered into pursuant to an off-site offer scenario, although on the facts the failure to do so did not cause Prato any loss.

Prato had full capacity to enter into the Swaps

Prato appealed against the finding of the High Court that the Swap did not breach Article 119 of the Italian Constitution and Article 41.2 of Law 448/2001. Rejecting Prato's appeal, the Court of Appeal held that the Swap was not indebtedness and could not breach Article 119, nor did the Swap involve new debt and fall within the scope of Article 41. Although not necessary to its decision, the Court of Appeal went on to confirm that even if Article 41 had applied to the Swap, it would not have failed the applicable Italian law "economic convenience" or "financial advantage" test as the initial MTM of a swap is not a relevant cost to be taken into account in that context.

COMMENT

The Court of Appeal's overall conclusion is that Prato had capacity to enter into the Swap, which is valid and remains on foot. Dexia was represented by Allen & Overy partner James Partridge, senior associate Helen Biggin and associate Sophie Nettleton.

The decision is a further endorsement by the Court of Appeal of the view that Article 3(3) is to be approached as a limited exception to the principle of party autonomy

to choose governing law. As we reported in our January 2017 Litigation Review article on the first instance decision, for commercial parties, the long reach of mandatory rules of the jurisdiction where a transaction is performed and their use as a means of contesting the validity of contracts remains a challenge, especially in the case of long-term contracts. This decision will offer some comfort to parties in search of contractual certainty. The Court of Appeal has held that key features of some capital markets transactions – ie the use of the ISDA standard form documentation, and the presence of a chain of back-to-back hedging transactions – establish that they are inherently international and should not be subject to mandatory rules of local law.

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CONSTRUCTION OF COMPETING JURISDICTION CLAUSES

Deutsche Bank AG v Comune di Savona [2017] EWHC 1013 (Comm), 5 May 2017

The Commercial Court has upheld an Italian local authority's jurisdiction challenge in respect of certain declarations relating to interest rate swaps entered into under an ISDA Master Agreement. At first instance, the judge ruled that some of the declarations in the English law and jurisdiction ISDA should fall to be decided in the English proceedings, which were issued first. However, notwithstanding an entire agreement clause and bespoke representations in the English law and jurisdiction ISDA, the judge ruled that certain of the declarations, which reflected the ISDA representations, should fall to be decided in more recent Italian proceedings issued by the defendant. Permission to appeal is currently being sought.

Parties should seek to ensure there are consistent governing law and jurisdiction clauses across suites of documents or otherwise include explicit reference to the relative scope of any competing jurisdiction clauses.

Background

Deutsche Bank AG (**DB**) and Comune di Savona (**Savona**) entered into two interest rate swaps in June 2007 under a 1992 ISDA Master Agreement, Schedule and two swap confirmations (the **Swaps**). The Swaps contained an exclusive English jurisdiction clause on the ISDA standard form (the **English Jurisdiction Clause**). Previously, in March 2007, DB and Savona had entered into a separate agreement for DB to provide certain unpaid assistance with the management of Savona's indebtedness (the **Convention**). The Convention was governed by Italian law and contained an exclusive jurisdiction clause in favour of the Courts of Milan (the **Italian Jurisdiction Clause**).

DB issued a protective claim against Savona in England in June 2016 (the **English Proceedings**) in light of the threat of potential legal action by Savona in Italy. DB served its claim on Savona in September 2016 seeking

12 declarations concerning the entry into, validity, enforceability, interpretation and performance of the Swaps. With one exception, the declarations closely tracked contractual representations in the ISDA Master Agreement.

In December 2016, Savona challenged the English Court's jurisdiction over six of the 12 declarations pursuant to Article 25 of the Recast Brussels Regulation 1215/2012 (**Article 25**) on the basis that they are subject to the Italian Jurisdiction Clause. Savona subsequently conceded on a limited basis that the English Court did have jurisdiction over the declaration reflecting the entire agreement clause in the ISDA Master Agreement. The remaining challenged declarations broadly focus on Savona's understanding of the Swaps, and the nature and extent of any advice provided by DB in relation to Savona's entry into them.

In March 2017, Savona commenced Italian proceedings against DB alleging, among other things, breaches of the Convention based on advice allegedly provided by DB concerning the Swaps (the **Italian Proceedings**).

HHJ Waksman QC upheld Savona's jurisdiction challenge in respect of the five remaining challenged declarations on the basis that DB's claims fell within the Italian Jurisdiction Clause.

The scope of the Convention

DB argued that the Convention did not impose any advisory obligations in respect of Savona's entry into the Swaps. The judge recognised that the Convention did seek to qualify the legal consequences of any advice given by DB thereunder (and that the effect of such qualifications was a matter of Italian law). The judge considered, however, that the essence of the Italian Proceedings related to advice given by DB, and a major part of that related to its role as adviser pursuant to the Convention.

The construction of the jurisdiction clauses

The judge set out his approach to considering the two jurisdiction clauses: (a) the Court should strive to construe the clauses as mutually exclusive in scope (ie not overlapping), even if this causes the jurisdictional fragmentation of a particular claim (*Monde Petroleum v Western Zagroz* [2015] 1 Lloyds Rep. 330); (b) there is no presumption that the later clause is intended to cut down the scope of the earlier clause (*Trust Risk v AmTrust Europe* [2015] 2 Lloyds Rep 154); and (c) each clause must be interpreted according to its own governing law.

The judge recognised that the English Jurisdiction Clause was part of an internationally recognised agreement, and referred to Briggs J's decision in *Lomas v Rixson* [2010] EWHC 3372 which stressed the importance of construing the standard terms of the ISDA Master Agreement so as to give them clarity and certainty. However, the judge held that the English Jurisdiction Clause had to be construed in the light of the prevailing legal context, which included the Convention and the Italian Jurisdiction Clause. If the effect of this was that the ambit of the English Jurisdiction Clause is more restricted than elsewhere then there is no rule of English law which prevents that.

Which jurisdiction clause applied to the challenged declarations?

The judge held that the "dispute" to which the challenged declarations relate must be regarded as Savona's claims in the Italian Proceedings. The judge found that, because Savona's claims in the Italian Proceedings were essentially concerned with DB's role as adviser, the dispute "is much more naturally" within the Italian Jurisdiction Clause than the English Jurisdiction Clause. This is on the basis that the Convention is concerned with DB as adviser while the Swaps are concerned with DB simply as counterparty. Although four of the challenged declarations closely tracked contractual representations in the ISDA Master Agreement, the judge found that this "did not irresistibly mean" that the dispute as to whether these declarations are correct was caught by the English Jurisdiction Clause. In respect of the final challenged declaration (which did not track an ISDA representation), the judge decided that this concerned matters which were the subject of the Italian Proceedings and therefore also outside the scope of the English Jurisdiction Clause.

COMMENT

The judge recognised that his analysis could produce some fragmentation (as Savona had accepted the English Court's jurisdiction in respect of the unchallenged declarations) but did not consider that it should be avoided at all costs.

In reaching his decision, it is also notable that the judge did not refer to *Deutsche Bank v Petromena* [2015] 1 WLR 4225, leading Court of Appeal authority

on the approach to Article 25. In that case Longmore LJ held that the Court is required (a) to have regard to the "thrust" of the claims advanced to determine the "dispute", and (b) to identify the "particular legal relationship" to which that "dispute" relates by considering the closeness of its connection to the different legal relationships between the parties.

The judge also declined to follow, and distinguished, the recent judgment of Ali Malek QC sitting as a Deputy High Court Judge in *Dexia Crediop SpA v Provincia Di Brescia* [2016] EWHC 3261 (Comm). In that case, considering similar facts, the judge found that declarations tracking the wording of the ISDA Master Agreement fell only within the scope of the ISDA jurisdiction clause. A similar approach was also taken by the Commercial Court and Court of Appeal in *Merrill Lynch v Verona* [2012] EWHC 1407 (Comm) and *Piemonte v Dexia* [2014] EWCA Civ 1298 in which the Court held that declarations based on representations made in an ISDA master agreement may be granted on the basis of contractual estoppel.

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Contract

LIMITED ROLE FOR *CONTRA PROFERENTEM* RULE IN THE INTERPRETATION OF COMMERCIAL CONTRACTS

Persimmon Homes Limited & ors v Ove Arup & Partners Ltd & anr [2017] EWCA Civ 373, 25 May 2017

In a dispute over the scope of an exemption clause in a construction contract, the Court of Appeal declined to apply the *contra proferentem* rule, emphasising its very limited role when interpreting a commercial contract between parties of equal bargaining power. The Court of Appeal noted *obiter* that the rule might still be relevant to indemnity clauses in commercial contracts.

Development of the *contra proferentem* rule for exemption and indemnity clauses

The *contra proferentem* rule, which requires any ambiguity in an exemption clause or indemnity clause to be resolved against the party who put the clause forward and relies upon it, originates in English law from the Privy Council decision in *Canada Steamship Lines Ltd v The King* [1952] AC 192. Over the years the *contra proferentem* rule has been extensively debated and the principles set out in *Canada Steamship* have tended to be applied more loosely in the form of guidelines rather than a strict rule.

In particular, the English court has favoured a more commercial, and less mechanistic, approach to the application of *Canada Steamship* when interpreting indemnity clauses and exemption clauses falling outside the scope of the Unfair Contract Terms Act 1977. In *K/S Victoria Street v House of Fraser (Stores Management) Ltd* [2011] EWCA Civ 904, the Court of Appeal held that the *contra proferentem* rule was rarely decisive as to the meaning of a commercial contract; the words used, commercial sense, and the documentary and factual contexts were normally enough to determine the meaning of a contractual provision. A similar approach was taken in the Court of Appeal's decision in *Transocean Drilling UK Ltd v Providence Resources PLC* [2016] EWCA Civ 372.

Exclusion of liability for asbestos

A consortium of property developers including Persimmon brought damages claims against Arup, the project consultant, for failing to identify large quantities of asbestos on a development site in South Wales. Among other defences, Arup relied on a contractual exemption clause which stated that "liability for any claim in relation to asbestos is excluded", and that "liability for pollution and contamination [is] limited to £5,000,000.00".

Persimmon argued that the exemption clause should be interpreted to apply only to liability for asbestos, pollution and contamination "caused" by Arup and that Arup's potential negligence in failing to identify asbestos would not be covered by the exemption clause.

First instance: interpretation of exclusion or limitation clauses essentially the same as any other clause

At first instance, Mr Justice Stuart-Smith referred to recent case law doubting the application of the *contra proferentem* rule to commercial contracts, and concluded that, as the law currently stood, the court's task was essentially the same when interpreting exclusion or limitation clauses as for any other contractual provision.

Applying these principles, the judge rejected Persimmon's arguments and held that the clauses in question were not restricted to liability for asbestos, pollution and contamination "caused" by Arup. They excluded all liability relating to asbestos whether relating to negligence or not. The judge noted that where contract terms (including exclusions or limitations of liability) were agreed by business people capable of looking after their own interests and allocating risks, then the court should be very slow to disturb or to characterise the agreement as unbusinesslike.

Court of Appeal: very limited role for the rule when interpreting commercial contract

The Court of Appeal upheld the judge's decision, which accorded with the natural meaning of the language used by the parties and business common sense. The Court of Appeal declined to apply the *contra proferentem* rule here. Referring to its previous decisions in *K/S Victoria Street v House of Fraser* and *Transocean Drilling v Providence Resources,* the Court of Appeal noted that the *contra proferentem* rule now had a very limited role in relation to commercial contracts negotiated between parties of equal bargaining power.

However, the Court of Appeal drew a distinction between the rule's application to exemption clauses and indemnity clauses. It accepted that, as a general principle, exemption clauses were part of the contractual apparatus for allocating risk in commercial contracts. There was no need to approach such clauses with a mind-set determined to cut them down. But the Court of Appeal did not extend the same reasoning to indemnity clauses and commented, *obiter*, that in so far as the *Canada Steamship* guidelines survived, they were now more relevant to indemnity clauses.

COMMENT

The Court of Appeal's decision in *Persimmon Homes v Ove Arup* confirms the increasing acceptance by the English court that commercial parties are entitled to agree to limit or exclude liability as a risk-allocation tool. While the Court of Appeal left open the possibility that the *contra proferentem* rule might still apply to indemnity clauses in commercial contracts, in practice it seems that for both exemption and indemnity clauses, much will turn on ordinary principles of interpretation of the wording in its context. This serves as a reminder of the value of careful drafting of such clauses during negotiations.

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Costs

PROFESSIONAL THIRD-PARTY LITIGATION FUNDER ORDERED TO PAY SECURITY FOR COSTS

The RBS Rights Issue Litigation [2017] EWHC 1217 (Ch), 23 May 2017

The High Court ordered security for costs against a commercial litigation funder but declined to do so in respect of a third-party funder who was not involved in litigation funding as a business. The case is interesting for its comparison of 'commercial' litigation funders and 'pure' litigation funders, and the factors the court takes into account when deciding which category a funder falls into.

Summary

The defendants sought security for costs from two foreign third-party funders at a late stage in the proceedings, following settlement of nearly all claims, on the basis that they could be liable in respect of an adverse costs order against the remaining claimants. One was a commercial litigation funder; the other claimed it only provided funds to assist associated entities, who were claimants. Both argued the defendants had not shown a real risk that any costs order would not be satisfied, the applications were too late, and that the security sought was excessive. The Court drew a clear distinction between 'pure funders' and commercial litigation funders, and ordered the commercial litigation funder to provide security for costs in a reduced sum, contingent on a cross-undertaking from the defendants. However, the Court determined it would not be just or appropriate to require the other third-party funder to provide security for costs.

Decision

There was no dispute that the Court has jurisdiction to order security for costs against a third-party funder. This power arises under the combined effect of s51 Senior Courts Act 1981 and CPR 25.14(2)(b). The exercise of this jurisdiction is fact-specific: case law can only provide general guidance. The Court identified five factors relevant to whether such an order would be appropriate and just:

Is it sufficiently clear that the non-party is to be treated as having in effect become, in all but name, a real party motivated to participate by its commercial interest in the litigation?

The reasons and motivations of the funder are important considerations. Courts will favour facilitating a 'pure funder' acting altruistically to enable access to justice, but will likely subject a commercial litigation funder to the costs and consequences of a commercial venture. However, many funders will fall somewhere in between that spectrum, and each case must be considered on its facts.

While Hunnewell Partners (BVI) Limited (**H**) was a commercial litigation funder, London and Northern Capital Partners Limited (**L**) asserted that it had never been involved in litigation funding as a business. Seven other entities associated with L (the **AEs**) were claimants in the proceedings, seeking over GBP100 million. L argued that it provided funds to facilitate access to justice for the AEs.

Although troubled by L's reluctance to disclose the terms of its arrangements, the Court concluded (on "admittedly sparse evidence") that the positions of H and L were "materially and relevantly different", and they should be treated differently for the purposes of the application. While L's line of business was not decisive, it did bear on the question of whether the funding was provided for commercial gain, and therefore the risks assumed by L. The Court resolved that L was closer to a 'pure funder' than a professional litigation funder. This was supported by the terms on which another of the AEs had provided funding: for no uplift, interest or

other return, to be repaid only after a substantial threshold recovery.

Is there a real risk of non-payment such that security against the contingent liability should be granted?

The risk of non-payment is not limited to non-payment by the claimant. Security can be ordered against non-parties "*whether or not the claimant is able to pay an adverse costs order himself*". Nevertheless, the claimant's ability to meet an adverse costs order remains relevant to assessing whether there is a real risk that such an order may not be paid. The Court held that both the possibility of alternative recourses and any difficulties in enforcing them are relevant considerations. The Defendants had sufficiently demonstrated a real risk of non-payment, as:

- ATE insurance was not sufficient to cover a potential adverse costs order; and
- a proportion of liability would fall on individual retail claimants of limited means (most of which were either deceased, pensioners, overseas, or blind trusts).

The Court emphasised that it would be unrealistic and unjust to underestimate the difficulties of recovering comparatively small sums from so many claimants.

The risk of non-payment by a third-party funder is also a relevant consideration. Adverse inferences may be drawn from a respondent's "deliberate reticence" to disclose information on their financial position. H and L were incorporated abroad, and not subject to public filing/inspection of accounts. As they declined to voluntarily disclose this information, their financial position was opaque. There was evidence that they were due to receive substantial sums as a result of the April settlements. However, there was no way for the Court to know whether even quite substantial receipts would result in funds available for payment of costs, and not be used, eg, to pay other creditors. Ultimately, the evidence was insufficient to dispel the impression of deliberate reticence, or the inference that H could not in fact demonstrate sufficient resources to meet an order for costs. The Court was not persuaded that confidentiality and secrecy were the true and predominant reasons for H's reticence. However, as L was more akin to a 'pure funder', it found L's reticence was more justifiable.

Is there a sufficient link between the funding and the costs for which recovery is sought to make it just for an order to be made?

Strict causation is not required; however an applicant will need to show "at least some causal link between the non-party's conduct and costs incurred".

Has the non-party been made sufficiently aware of the risk of liability for costs, either by express warning, or by reference to what a party in its position should be taken to appreciate as the inherent risks?

The importance of a warning will vary from case to case. The lack of an express warning is unlikely to carry much weight in respect of a commercial litigation funder. The Court cautioned that "it is not for the Court to protect a party from inherent business risks of which it should be well aware".

H was assumed to know risks inherent in its own line of business, and thus to have appreciated the risk of adverse costs liability or being ordered to provide security. However, this could not necessarily be said of L, which contended that it did not anticipate or expect such eventualities. The timing of the funding provided was also relevant. As L had provided funds "almost on the eve of the trial", the Court accepted that the possibility of an order security for costs may not have been contemplated or provided for. It considered that it would not be just to require L to provide security for an obligation it cannot be assumed to have envisaged or provided for.

Are there factors, such as delay in making an application for security, or likely adverse effects such as to tip the overall balance against making the order?

While an application for security can be made at any stage, the Court will be concerned not to allow this to act as an instrument of oppression, particularly where the defendant's failure to meet a claim may have materially caused the claimant's impecuniosity. The Court must carefully balance the reasons for making the order, and the considerations of overall justice. The Court considered that lateness does not necessarily connote unjustified delay: it is important to assess the reason and its prejudicial effect.

Here, there was extreme delay. However, this was not fatal to the application for security. The settlements had changed the risk profile of the claimants. It had also become apparent that the claimants' ATE cover was

materially inadequate (contrary to the public impression created by SG at all times until December 2016). As a commercial litigation funder H should have been fully aware of the position regarding ATE cover, and either get to the bottom of any uncertainty, or incur the risks of not doing so.

The Court expressed its concerns about the disparity and magnitude of the Defendant's costs and the risk that they might have made it impossible for the claimants to obtain ATE cover (which in turn triggered the application for security). However, it appreciated the complexity and size of the case, and that security was only sought in relation to costs post-December 2016. It stressed that costs must be proportionate to be recoverable and that parties "are free to pay for a Rolls-Royce service but not to charge it all to the other side".

While the Court declined to order L to provide security, it did not consider it just for what might equitably be considered 'L's share' of the costs to fall on H. It calculated an appropriate figure, concluding H should be required to pay approximately 38% of the sums sought. Finally, the Court required a cross-undertaking from the Defendants, as a means of ensuring compensation in case it became apparent the order should not have been made.

COMMENT

This decision confirms the power of the courts to order security for costs against third parties, and underscores that the exercise of this power will depend on the specific facts of each case. It emphasises the different treatment of 'pure funders' and commercial litigation funders, and the types of "inherent business risks" that they will be taken to have assumed. On the facts, the lack of sufficient ATE cover was also particularly relevant. It further illustrates that, while a funder's line of business is not decisive, the courts will be more willing to order security against a commercial litigation funder. The decision may also encourage commercial litigation funders to seek a cross-undertaking when faced with an application for security for costs.

Notably, the Defendants made clear that they might in due course seek in principle 100% of any costs awarded from H and L, and argue against the application of any "*Arkin cap*". Should such circumstances arise, we may well see further developments in these proceedings.

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Defamation

SOCIAL MEDIA IN LITIGATION

Monroe v Hopkins [2017] EWHC 433 (QB), 10 March 2017

A high-profile libel claim for defamatory statements made on Twitter provides a study on how to apply the law of defamation in the social media age and highlights risks (and opportunities) that litigants or potential litigants should manage relating to use of social media.

The claimant (**Monroe**) was a food writer and blogger. The defendant (**Hopkins**) was a well-known newspaper columnist. In May 2015 there was an anti-austerity protest in London. During this protest, the Memorial to the Women of World War II in Whitehall was vandalised, causing public outrage. There was no suggestion Monroe was in any way involved, nor supported the vandalism. However two subsequent Tweets by Hopkins appeared to suggest that Monroe was in some way involved with, or condoned, the vandalism. The first was deleted before the second was published.

- First Tweet: "@MsJackMonroe scrawled on any memorials recently? Vandalised the memory of those who fought for your freedom. Grandma got any more medals?"
- Second Tweet (on the same day as the first, and after the first had been deleted at Monroe's request): "Can someone explain to me – in 10 words or less - the difference between irritant [Laurie Penny] and social anthrax [Jack Monroe]."

The meaning of a Tweet

For an action in libel to succeed, it must be shown that a published statement (i) has a tendency to defame and (ii) per section 1 of the Defamation Act 2013, that the statement causes, or is likely to cause, serious harm to the claimant's reputation (the **serious harm requirement**).

The court, in deciding the meaning of the first and second Tweets, relied on the principles set out in *Jeynes v News Magazines Ltd* [2008] EWCA Civ 130. Applying the overarching principle of reasonableness to Twitter meant that the court must take into account the whole Tweet and the context in which the ordinary reader would read that Tweet. This context could include parts of a larger Twitter conversation which the ordinary reader was likely to have read.

Warby J held that, while a reasonable reader would not have understood the Tweets to literally mean Monroe herself had defaced the war memorial, the natural and ordinary meaning of the first Tweet (and the innuendo meaning of the second Tweet to those knowing the surrounding facts) was that Monroe condoned and approved of vandalising the war memorial.

Given this meaning, the court held it had no doubt that the first and second Tweets were defamatory in nature (alleging Monroe supported a criminal act which had received widespread public condemnation).

Serious harm

The judgment was also notable for its application of the serious harm requirement under the Defamation Act 2013 to social media platforms.

A key part of Hopkins' defence was that no serious harm had been caused by the Tweets. Of particular note was the argument that the first and second Tweets were transient in nature – particularly relevant given the fast-paced nature of Twitter. Rejecting this, the Court held that the key consideration was the impact a statement had – not how long people were exposed to the message.

Following assessment of the extent of publication and consideration of quantum, the court awarded Monroe GBP24,000 (GBP16,000 for the first Tweet and GBP8,000 for the second Tweet) for damage to reputation and distress caused.

COMMENT

This is not the first libel case relating to statements made on Twitter (see in particular *McAlpine v Bercow* [2013] EWHC 1342 (QB)), nor is it likely to be the last.

The costs of Tweeting first and thinking later have been emphasised: the first Tweet in this case was publically viewable for less than two and a half hours before being deleted.

The judge flagged issues in discovery caused by the deletion of: (i) the first Tweet by Ms Hopkins (at Monroe's request); and (ii) much of Monroe's Twitter records. Warby J noted these deletions highlighted "the responsibility of a litigant to retain and preserve material that may become disclosable, and the responsibility of a solicitor to take reasonable steps to ensure the client appreciates this responsibility and performs it".

This warning also feeds into a broader point for practitioners. Courts are not shying away from considering the actions of individuals (or indeed employees) on social media when relevant to a case. Such actions may impact everything from discovery to settlement offers (indeed in this case Monroe had made an offer not to sue provided the first Tweet was removed and a sizeable donation to charity was made –which the court regarded as an open offer to settle, even though it was contained in a Tweet) to the assessment of the level of damages suffered by a claimant.

For commercial parties, an errant Tweet could be relevant to what parties understood a statement or provision to mean. Where appropriate, ensure consideration is given to social media accounts when providing guidance and retention notices to employees. When embarking on litigation involving an individual with a highly active online presence, monitoring their social media accounts may be prudent.

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Privilege

THIRD-PARTY ACCESS TO WITHOUT PREJUDICE NEGOTIATIONS

EMW Law LLP v Halborg [2017] EWHC 1014 (Ch), 4 May 2017

Without prejudice communications should be disclosed to a third party because two exceptions to the without prejudice rule applied (the "concluded settlement agreement" and "reasonableness of mitigation" exceptions). Previous case law in this area involved one of the parties to the without prejudice communications (rather than a third party) relying on these exceptions. The court drew a distinction between the waiver of without prejudice privilege (which must be done jointly) and merely "showing" a without prejudice communication to a third party (which, the court said, can be done unilaterally).

Mr Halborg, a solicitor, was instructed by his parents and a family company (the **Halborg Claimants**) in relation to a dispute between the Halborg Claimants and a firm of architects (the **Architects**). With the agreement of the Halborg Claimants, Mr Halborg instructed another firm of solicitors, EMW Law LLP (**EMW**), to assist him in the conduct of the case. EMW was retained on the basis of a conditional fee agreement (the **Agency CFA**) which provided that it would only be paid once Mr Halborg had recovered EMW's costs from the Architects.

The Halborg Claimants issued proceedings against the Architects. These proceedings were settled by a £350,000 Part 36 offer from the Architects. As a result, the Architects became liable to pay the Halborg Claimants' costs. Mr Halborg entered into without prejudice negotiations with the Architects' solicitors to settle these costs, in relation to which a bill of cost was served which sought just over £1.3 million (including £123,590 for EMW's "agency charges").

No amount was paid to EMW. It therefore started these proceedings against Mr Halborg for breach of various implied terms in the Agency CFA which it claimed resulted in EMW not being paid.

Without prejudice communications sought by EMW

On disclosure, Mr Halborg withheld his communications with the Architects' solicitors on the recovery of costs on the basis they were protected by without prejudice privilege. EMW argued that the normal without prejudice rule did not apply as what was at issue was whether a settlement agreement had been reached and/or the mitigating steps taken by Mr Halborg in relation to settlement.

The matter came before Newey J in the High Court on appeal.

Without prejudice reminder

The court noted that the without prejudice rule operates to protect negotiations genuinely aimed at settlement

from being given in evidence. This means that such negotiations are immune from disclosure.

The rule can continue to apply even after a compromise has been reached and its implications are capable of extending beyond the parties to the relevant negotiations. The privilege is a joint one and can therefore only be waived jointly. It is not open to one of the parties to the negotiations to waive the privilege unilaterally.

There are, however, settled exceptions to the without prejudice rule. This case considered two exceptions, which provide that without prejudice communications are admissible (and discloseable):

- for the purpose of determining whether a settlement agreement has been concluded (the **concluded settlement agreement exception**);
- where there is an issue as to whether a party has acted reasonably in mitigating his loss by virtue of his settlement negotiations and conduct (the **reasonableness of mitigation exception**); and
- the second exception encompasses the facts in *Muller v Linsley Mortimer* [1996] 1 PNLR 74.

Both exceptions apply

The court held that both the concluded settlement agreement exception and the reasonableness of mitigation exception ("or, another, comparable, exception") applied.

Concluded settlement agreement exception

The concluded settlement agreement exception applied as there was in fact a dispute as to whether a settlement agreement had been reached. The court dismissed Mr Halborg's concerns that allowing a third party to rely on this exception would mean that a stranger to without prejudice negotiations could obtain communications which the parties themselves were entitled to assume enjoyed the protection of privilege. The court noted that "while a party to without prejudice negotiations is generally entitled to assume that the negotiations will not generally be capable of being deployed in Court proceedings without his consent he has no absolute assurance of that" given there are exceptions to the rule. The risk of the concluded settlement agreement exception applying is not "significantly increased if it is understood as allowing not merely a party to the negotiations, but someone else with a legitimate interest in their outcome, to rely on it."

Reasonableness of mitigation exception

The court also held that the reasonableness of mitigation exclusion applied.

The judge said that "justice clearly demands" that there is an exception "(whether that encompassing the facts of the *Muller* case or another, comparable, exception)" because:

- It would be difficult for EMW's claim to be justiciable without disclosure of the without prejudice communications.
- Mr Halborg made reference to his without prejudice negotiations in his defence (when he explained to EMW that the Architects' solicitors "ascribed no value at all to [EMW's] work").
- There was "no likelihood" that recognising that an exception should apply here would deter parties seeking to settle as they will, if well informed, be aware of the two exceptions to the without prejudice rule relevant to this case.
- There is a persuasive argument that if a client (like the Halborg Claimants) authorises his solicitor to employ an agent on the basis that the agent's remuneration depends on what agreement as to costs is reached with the other side, "the client can hardly complain if his negotiations with the opposing party are susceptible to being revealed to and relied on by the solicitor-agent".
- Where there is a need the court could make an order to restrict the use of a disclosed document, even where read out in open court.

Waiver v "showing" distinction

The judgment records that there was some debate during the hearing as to whether a party to without prejudice communications could "show" a third party documents without obtaining the consent of the counterparty to that communication. The court noted that it was accepted that a waiver of without prejudice privilege can only happen with the consent of both parties, which protects the negotiations from unilateral disclosure. However, the court tentatively considered ("[t]he answer, I think, must be…") that a party to without prejudice negotiations is

free to "show" them to someone else if he so chooses, "at least if there is a legitimate reason for doing so". The judge said that if the position were otherwise, a litigant "might find himself unable to provide relevant documents to, say, an expert unless and until the other side agreed, which would be absurd."

COMMENT

This case is interesting in that it has allowed a third party to make use of the concluded settlement agreement and reasonableness of mitigation exceptions, despite no party to the negotiations seeking to rely on the without prejudice material. Although the judge in this case came to the view that allowing a third party with a legitimate interest in negotiations to rely on these exceptions will not deter parties from settling, there may be cases where that risk needs to be given serious consideration and this may affect what is said in negotiations (although its effect may be tempered to some extent by obtaining a court order to prevent the collateral use of the material). We understand that an application for permission to appeal has been filed in relation to this judgment.

The judge's distinction between waiver of without prejudice and merely "showing" a communication to a third party is troubling. It is generally accepted that parties to without prejudice negotiations owe each other a private law duty of confidentiality (although that duty is subject to certain exceptions). Despite this, the judgment does not address how "showing" a without prejudice communication to a third party would not be a breach of such a duty, beyond suggesting that there needs to be a "legitimate reason" for "showing" the documents to the third party. If this decision is seen as broadening the circumstances in which a party can "show" without prejudice communications to third parties, there is a risk it could act as a significant disincentive to engaging in settlement negotiations, in particular in cases where a party is aware that third parties may have similar claims or is concerned about adverse publicity. If settlement negotiations are particularly sensitive or where there is a clear risk of harm if the details of those settlement negotiations are shown to third parties, parties may wish to consider expressly agreeing that their negotiations are confidential and cannot be shown unilaterally to third parties to bolster their legal rights and help manage counterparty behaviour.

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Service

EFFECT OF FAILURE TO RENEW APPOINTMENT OF A PROCESS AGENT FOR SERVICE OF PROCESS

Aquila WSA Aviation Opportunities II Ltd v Onur Air Tasimacilik As [2017] EWHC 1259 (Comm), 12 April 2017

A defendant's failure to renew a process agent's appointment did not affect a claimant's right to serve a claim form at the address of the original process agent (which had become a building site) because the contract provided that the process agent was appointed 'irrevocably'.

A defendant's failure to renew a process agent's appointment did not affect a claimant's right to serve a claim form at the address of the original process agent (which had become a building site) because the contract provided that the process agent was appointed 'irrevocably'.

A process agent clause is a common type of boilerplate clause in international commercial contracts. It simplifies service of legal process on a foreign counterparty by agreeing upfront who is authorised to accept service on that party's behalf. This can save time and costs where the potential defendant is based outside the jurisdiction. This case concerns a process agent appointment that lapsed before a dispute arose.

Aquila, an asset finance company, entered a lease agreement with Onur Air, a Turkish airline. The agreement contained a process agent clause which provided that Onur Air had irrevocably appointed a company (**CSC**) as its agent for service in relation to any proceedings and that if the agent's appointment ceased to be effective, Onur Air shall, as soon as reasonably practicable, appoint another agent. Onur Air sent Aquila a copy of a letter which confirmed the appointment of a company (**CSC UK Limited**) as process agent for one year. A dispute arose and Aquila issued a claim form in the English courts seeking USD 9 million.

Aquila sent a copy of the claim form by email to Onur Air's address in Turkey, which Aquila accepted did not constitute effective service. Aquila then attempted to serve on CSC UK Limited at its address in London, but it was unable to do so because the address was a building site and it transpired that there was no company or entity called 'CSC'. Aquila then attempted to serve the claim form on another company (**CSC Limited**), which was not in existence at the time the contract was agreed but was formerly registered at the same address as CSC UK Limited, at its new address by handing it to an individual on the premises. The relationship between CSC Limited and CSC UK Limited was unclear.

Onur Air sought to set aside the claim and/or service of the claim, arguing that service was not effective because CSC UK Limited's appointment had lapsed and that the wrong process agent (CSC Limited) was served. In response, Aquila sought an order declaring that service was valid, permitting alternative service on CSC Limited under CPR 6.15 or rectifying an error of procedure under CPR 3.10.

Service on a building site would have been possible as the process agent's irrevocable appointment was still valid

Cockerill QC (sitting as a Deputy High Court Judge) found that the service agent clause appointed a CSC entity to be designated and the confirmation of appointment letter defined that entity as CSC UK Limited. Aquila's right to effect service under the contract could not be affected by the fact that Onur Air had appointed CSC for one year and then failed to renew the appointment. The parties' agreement could not be revoked by a letter confirming appointment to which Aquila was not a party (*DVB Bank SE v Isim Amin Ltd* [2014] EWHC 2156 (Comm)). The contractual position between Aquila and Onur Air was unchanged. The process agent clause in the contract stated that the process agent was appointed irrevocably and this intention was supported by the need for a back-up process agent, where necessary, in order to allow service in the jurisdiction if the original agent was not able to act. Unless and until the identified process agent ceased to exist, as between Aquila and Onur Air, the process agent's appointment remained valid and it was a matter for Onur Air if the agent ceased to act or move offices. Any looser construction of the words "ceases to be effective" would subvert the meaning of "irrevocable". The judge therefore concluded that Aquila could have validly served CSC UK Limited at its original address, even though it was a building site.

Service on the wrong process agent was good service (or a procedural error capable of remedy)

In order for the judge to make an order permitting alternative service under CPR 6.15, the judge had to be satisfied that there was good reason to make the order. Applying Popplewell J's summary of the relevant cases in *Societe General v Goldas Kuyumculuk Sanayi Ithalat Ihracat AS* [2017] EWHC 667 (Comm) the judge found that Aquila had demonstrated good reason why the claim form had not been served on Onur Air "with all the perfection of form which is technically required":

- this was "plainly" a case where Onur Air had learned of the existence and content of the claim form. Onur Air had filed an acknowledgement of service indicating its intention to contest jurisdiction less than two weeks after the claim form was issued;
- while Onur Air had not been "playing technical games overall," its position on service at an address which was the same address as the nominated process agent was "certainly technical" and Onur Air's argument about expiry of the process agent's appointment essentially relied on a breach of its obligation to appoint a new agent under the process agent clause;

- although the judge had found that Aquila could have served and could probably still serve the claim form on CSC UK Limited before it expired, Onur Air's focus appeared, until recently, to have focused primarily on the expiry of the agent and therefore, earlier service on CSC UK Limited would not have avoided this challenge. Onur Air also failed to appoint a new agent, despite a request from Aquila that it do so and despite the terms of the agreement; and
- Aquila's attempts at service were prompt, as was its application under CPR 6.15 following Onur Air's jurisdictional challenge, and Aquila had sought to list the hearing before the claim form expired.

On the facts, the judge found that Aquila had demonstrated good reason for the order and, even though there was still time for Aquila to re-serve the claim form, ordered that service on CSC Limited was good service under CPR 6.15(2) on the basis that to order further steps to be taken to effect service would only increase costs, which "would hardly be in line with the overriding objective".

In addition, the judge found *obiter* that, had she not ordered that the service on CSC Limited was good service under CPR 6.15, she would have been inclined to conclude that service on the process agent was a procedural error falling within CPR 3.10 so as to permit an order to be made remedying the error.

COMMENT

This decision will give potential claimants some comfort that the English courts will be reluctant to allow a foreign defendant to get out of an agreement to "irrevocably" appoint an English process agent for service in the jurisdiction and that the courts will not be persuaded by "technical" arguments by a defendant to avoid formal service in circumstances where the defendant was fully aware of the claim against it.

The decision is also a good reminder of why it is sensible to include clearly drafted English process agent clauses in contracts with foreign counterparties. Process agent clauses make service much easier and therefore save time, cost and hassle.

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SERVICE ON AGENT NOT EFFECTIVE FOR PURPOSES OF CPR 6.9

Noble Caledonia Ltd v Air Niugini Ltd [2017] EWHC 1095 (QB), 12 May 2017

Where an overseas company's agent transacts in England and Wales, that company is not carrying on its activities in the jurisdiction for the purpose of serving a party under Rule 6.9 of the Civil Procedure Rules (the CPR). The serving party must therefore take steps to serve out of the jurisdiction.

The claimant (**NC**) is a tour operator that operates cruises in various parts of the world. The defendant (**ANG**) is the national airline of Papua New Guinea. This claim relates to an ANG flight from Singapore to Port Moresby, which was to carry a number of NC's clients to embark on a cruise ship at Port Moresby, but which failed to be available for take-off in time for them to do so. The flight was arranged by NC through its UK-based agent, Flight Directors Scheduled Services Limited (**FDL**), which is claimed to form the contractual basis for the relationship between NC and ANG.

NC sought to bring a claim in England against ANG for breach of contract. This judgment deals solely with the preliminary issue of whether NC had properly affected service on ANG under Rule 6.9 of the CPR.

CPR 6.9

CPR 6.9 deals with service of the claim form where the defendant has not given an address at which it may be served. For the purpose of this case, the relevant part of CPR 6.9 provides that service must be made on an overseas company at "any place within the jurisdiction where the corporation carries on its activities; or any

place of business of the company within the jurisdiction," and when there is no such place, then service must be made out of the jurisdiction. It was common ground between the parties that the judge's decision would be centred on whether ANG carried on its activities within the jurisdiction.

The parties' arguments

NC purported to serve the claim form on ANG by way of personal service on the general manager of FDL, who indicated that she was not accepting service but would pass the documents on to ANG.

NC's argument that service was valid was based on certain actions and behaviours of FDL's Head of Sales and Marketing, who was also Head of Sales in relation to the general sales agency that FDL operated on behalf of ANG. NC contended that she was effectively carrying on the activities of ANG in the UK, that she had primary responsibility for the provision of ANG services in the UK and that she held her actions out as being those of ANG. For instance, the individual prefaced FDL's office address with "Air Niugini GSA" and implied she was an employee of ANG in correspondence with NC. Accordingly, NC argued that this showed ANG as present in the jurisdiction.

ANG relied on a string of authorities that demonstrate the English court's reluctance to confirm that an overseas company carries on its activities within the jurisdiction. In particular, in his judgment Gilbart J cited the criteria for determining whether an overseas company had "presence" in the jurisdiction as set out by Slade LJ in *Adams* v *Cape Industries*, in summary:[1]

- the English Courts will likely treat an overseas company as having presence in the jurisdiction only if either:
  - it has established and maintained at its own expense a fixed place of business of its own in the jurisdiction and for more than a minimal period of time has carried on its own business at or from such premises by its servants or agents; or
  - a representative of the overseas company has, for more than a minimal period of time, been carrying on the overseas company's business in the jurisdiction at or from some fixed place of business.

In either of the two above cases, presence will likely only be established if it can fairly be said that the overseas company's business has been carried out at or from that business address. In respect of the second limb, in particular, the court will conduct an analysis of the functions the representative has been performing and all aspects of the relationship between him and the overseas company.

In particular, a non-exhaustive list of questions is to be asked, including, among other matters, an enquiry about the reimbursement of the representative, the degree of control exerted by the overseas company and whether the individual can bind the overseas company.

ANG contended that FDL's activity did not amount to a presence in the jurisdiction for the purpose of CPR 6.9, that FDL only ever acted as ANG's agent for ticket sales and that nothing it did could be described as the "activities" of ANG. The reality was that FDL worked for several principals and made similar arrangements surrounding telephone numbers and business cards with them as it did with ANG. Further, it was limited in its ability to enter into contracts or exercise any real autonomy in relation to negotiating contractual terms or pricing.

Judgment

On the facts of this case, Gilbart J found that service was not validly effected under CPR 6.9. Points of particular importance for him were that:

- the relationship between ANG and FDL had to be considered in the context of parties operating in the airline industry. Therefore, the terms of the agreement between the two parties had to be considered. This particular agreement limited FDL's discretion and provided that they were paid only on commission; and
- the facts indicated a lack of control by ANG over FDL's actions. Previous cases have held that where business is done through an agent, the less freedom the agent has to negotiate contracts, the less likely the 'presence' test is to be met.

Therefore, Gilbart J held that NC would have to serve proceedings on NC out of the jurisdiction.

COMMENT

This case provides a cautionary tale to persons seeking to effect service on an overseas company through a third-party agent in England and Wales. The wording "*Any place within the jurisdiction where the corporation carries on its activities; or any place of business of the company within the jurisdiction*" in CPR 6.9 should be construed narrowly. It should be seen as a gateway through which to serve on an overseas company only where it is clear that the overseas company carries out its activities from a specific location within a jurisdiction. This case provides helpful clarification on the relevant test and confirms that an agency relationship alone is not enough to satisfy the test under CPR 6.9.

The concept of a company "carrying on" business of some sort in the UK is a familiar one, used in various The concept of a company "carrying on" business of some sort in the UK is a familiar one, used in various ways in certain pieces of UK legislation, for example section 7 of the Bribery Act 2010, which provides for the exercise of jurisdiction where an entity "carries on… part of a business, in any part of the United Kingdom". This is intended to (and does) have extra-territorial reach, and for public policy reasons the standard to be met may be lower than that applied by Gilbart J in this case for the purpose of establishing jurisdiction. Gilbart J's approach is in keeping with the common law rule that having an agent somewhere is not akin to "carrying on" its business there.[2] As such, although the factors taken into account in *Noble Caledonia* will be relevant to an assessment of whether an overseas company is carrying on its business in the jurisdiction for any purpose, the standard to be met for CPR and jurisdiction purposes may be higher.

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1 *Adams v Cape Industries* [1990] 1 Ch 433 (CA).
2 *Grant v Anderson* [1892] 1 Q.B. 108.

Tort

BANK HELD TO HIGHER DUTY DESPITE NO ADVISORY RELATIONSHIP

Philip Thomas & anr v Tridos Bank NV [2017] EWHC 314 (QB), 2 March 2017

Even where no advice was given, a bank's duty of care to its customer was higher than a duty not to misstate facts and extended to explaining the financial implications of certain loans. The decision suggests that, in certain circumstances outside an advisory relationship, lenders may be required to explain certain risks and features of financial products to their customers prior to sale.

Philip and Helen Thomas (the **claimants**) owned a farming business. In 2006, the claimants transferred their borrowings to Tridos Bank NV (**Tridos**). The claimants' borrowing from Tridos was in the form of two variable rate loan agreements of GBP300,000 and GBP1.15 million (the **Variable Loans**).

In 2008, the claimants became concerned about the impact of increasing interest rates on their Variable Loans and discussed with Tridos the possibility of fixing part of their debt. These discussions took place by telephone and in writing. During these discussions, the claimants asked whether the financial penalty for fixing the Variable Loans and then redeeming them early

would be in the region of GBP10,000- 20,000. Tridos did not answer, correct or refute this, even though in reality the figure was closer to GBP94,000. Following these discussions, in June 2008, the claimants fixed a significant portion of their borrowing in two tranches for 10 years (the **Fixed Loans**).

In September 2008, interest rates began to fall sharply as a result of the global financial crisis. Now concerned with the level of repayments required under the Fixed Loans, the claimants asked Tridos about the penalties they would incur if they redeemed the Fixed Loans early and restructured the debt at a lower interest rate. The early redemption fee for the Fixed Loans was calculated at GBP94,205.47 (later discounted to GBP54,691.50). This was far greater than the GBP10,000-20,000 the claimants thought they would be charged.

The claimants sued Tridos, alleging that it had:

- owed the claimants a duty to explain the financial consequences of redeeming the Fixed Loans before the end of their ten year term, and that it breached that duty; and
- misrepresented what the financial consequences of early redemption of the Fixed Loans would be by failing to correct or refute the claimants when they queried whether the early redemption fee would be in the region of GBP10,000-20,000.

Decision

Deciding the case in favour of the claimants, the court held that, although the relationship between the parties was not an advisory one:

- at a minimum, Tridos owed the claimants a duty not to misstate any facts upon which they might have been expected to rely. This is the "*Hedley Byrne v Heller*" duty which applies when a bank provides information rather than advice;[1] and
- a higher, "intermediate", duty could exist outside an advisory relationship in certain circumstances.[2] The existence of this intermediate duty would depend on the specific facts and whether it was appropriate to impose that duty as a matter of public policy.

Business Banking Code

Tridos had explained in its product literature and certain correspondence with the claimants in relation to the Fixed Loans that it subscribed to the Business Banking Code (**BBC**). The BBC included a promise that Tridos would treat its business customers reasonably when providing them with a product and that this promise included: (1) giving the customer information about the product in plain English; and (2) explaining the financial implications of the product. This fairness commitment stated that "customers should be given a balanced view of products so that they have an accurate understanding of the financial implications".

The court found that because:

- Tridos had subscribed (and advertised its subscription) to the BBC to the claimants;
- there were no disclaimers, "basis clauses" or exclusions in the terms and conditions which applied between the claimants and Tridos which would lead to the conclusion that Tridos was not willing to assume responsibility for its promises in the BBC; and
- the claimants had questioned Tridos about the potential financial impact of redeeming the Fixed Loans early,

Tridos adopted a higher duty of care to the claimants (in line with the fairness commitment in the BBC) to explain to them the financial implications of fixing the Fixed Loans. This duty came into existence because the claimants had specifically questioned Tridos about the potential financial implications of early redemption of the Fixed Loans. Tridos did not have a duty to volunteer information.

His Honour Judge Havelock Allan QC explained that, while Tridos was not required to provide the claimants with a "comprehensive tutorial" about the financial implications of early redemption of the Fixed Loans, the bank was, at a minimum, required to explain to the claimants: (1) that the rate could be fixed for a period (whether in months or years, and whether any minimum length of time); (2) whether the available fixed rates could be found (eg on the internet); (3) what those rates

represented (the forward cost of money); (4) the effective rate that would be payable (ie the current swap ask rate for the period of the fix plus the bank's margin, if any); and (5) the financial consequences of terminating the fixed rate before the end of the period.

The Court also found that Tridos' failure to clarify the potential financial penalty for early redemption of the Fixed Loans when Mr Thomas asked whether the financial penalty would be GBP10,000-20,000 gave rise to a misrepresentation which influenced the claimants' decision to enter into the Fixed Loans.

COMMENT

This case is a useful illustration of the circumstances in which a bank or financial institution may be held to a higher duty than one which requires them not to misstate facts, even where there is no advisory relationship.

This duty may extend to a duty to explain the features and risks of a product, particularly in circumstances where the bank or financial institution has signed up to a voluntary code of practice which requires fairness commitments such as those relevant in this case.

Where banks or financial institutions have signed up to a voluntary code of practice, they should consider how that code interacts with specific product terms and conditions, such as basis clauses or exclusions.

The code of practice referred to this case as the BBC is now the Lending Code. The Lending Code will be superseded on 1 July 2017 by the Standards of Lending Practice.

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1 *Green & Rowley v Royal Bank of Scotland* [2012] EWHC 3661.

2 Citing with approval the decision of Judge Moulder in *Thornbridge v Barclays Bank* [2015] EWHC 3430 (QB).

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Key contacts

If you require advice on any of the matters raised in this document, please call any of our partners or your usual contact at Allen & Overy.

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