INTERNATIONAL FINANCE: SPRING 2011

Materials Chapter 3

ISSUES IN SYNDICATED LOAN AGREEMENTS WITH INTERNATIONAL ASPECTS I

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EURODOLLARS, EUROCURRENCY LOANS AND LIBOR

We will focus on the **eurocurrency** loan aspects of the agreement we are studying.[2] Please note the eurodollar interest provisions of this loan facility agreement The interest rate for eurocurrency loans is basically the eurocurrency rate plus a margin (in the agreement this is referred to as the “Applicable Rate”).[3] The eurocurrency rate is sometimes referred to as Libor,[4] which stands for “London Interbank Offered Rate” and is the rate of interest at which banks could borrow funds from other banks, in marketable size, in the London interbank market. Libor is the rate of interest which applies to eurocurrency deposits, which are deposits of currency outside the jurisdiction to which the currency belongs.[5] Originally, the currency in which eurocurrency deposits were denominated was the US dollar because there was significant interest in holding deposits denominated in dollars (because the dollar was the reserve currency), and some depositors had an interest in holding dollars outside the US for various reasons. Later, eurocurrency deposits developed for other currencies (euroyen deposits, for example).

The term eurocurrency needs to be distinguished from the euro, which is the currency of some of the Member States of the European Union. The single currency is an aspect of economic and monetary union in the EU. Originally 11 Member States formed the euro zone and it now includes seventeen of the twenty-seven Member States. The eurozone countries are Belgium, Germany, Ireland, Spain, France, Italy, Luxembourg, the Netherlands, Austria, Portugal, Finland, Greece, Slovenia, Cyprus, Malta, Slovakia and Estonia. Members of the EU, and more specifically of the

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[2] Syndicated Loan Agreement between International Assets Holding Corporation and Bank of America and other Lenders (October 1, 2010) available at http://www.sec.gov/Archives/edgar/data/913760/000118143110053284/rrd289999_33283.htm.

[3] Section 2.08 provides: “(a) Subject to the provisions of subsection (b) below, (i) each Eurodollar Rate Loan shall bear interest on the outstanding principal amount thereof for each Interest Period at a rate per annum equal to the sum of the Eurodollar Rate for such Interest Period plus the Applicable Rate”.

[4] See the definition of the Eurodollar Base rate which refers to BBA Libor.

[5] “Formally, a eurodollar is a US dollar deposit, typically a 30-, 90- or 180-day time deposit, which is placed in a bank located outside the United States (often called a “eurobank”). Neither the nationality of the bank nor the location (or nationality) of the supplier of funds is relevant. What is relevant is the location of the bank accepting deposits. Thus, a US dollar deposit by a US manufacturing firm in a branch of a US bank in London is considered a eurodollar, while a US dollar deposit by a French company in a German bank in New York is not.” BIS Quarterly Review, Sept 2004, p 68, note 2.

eurozone, are supposed to co-ordinate their economic policies, but the financial crisis exposed weaknesses in the eurozone, initially with respect to Greece. Greece has received financial support from other Euro area countries of €80 billion, has a stand-by arrangement with the IMF, and has been implementing structural reforms.[6] Ireland has also received financial support from the EU and IMF and has implemented reforms.[7] The EU is discussing reforms to its model of economic governance, involving "fiscal discipline, notably through a stronger Stability and Growth Pact.. broadening economic surveillance to encompass macro imbalances and competitiveness.. deeper and broader coordination.. a robust framework for crisis management ..stronger institutions and more effective and rules-based decision making".[8]

When the eurodollar deposit market developed, interest rates for eurodollar deposits in London were higher than domestic interest rates in the US largely because domestic regulation of interest rates in the US did not apply in London.

Milton Friedman described eurodollars as follows:

...Euro-dollars ... are deposit liabilities, denominated in dollars, of banks outside the United States. ...Funds placed with these institutions may be owned by anyone- U.S. or foreign residents or citizens, individuals or corporations or governments. Euro-dollars have two basic characteristics: first, they are short term obligations to pay dollars; second, they are obligations of banking offices located outside the U.S....

A homely parallel to Euro-dollars is to be found in the dollar deposit liabilities of bank offices located in the city of Chicago-which could similarly be called "Chicago dollars." Like Euro-dollars, "Chicago dollars" consist of obligations to pay dollars by a collection of banking offices located in a particular geographic area....

The location of the banks is important primarily because it affects the regulations under which the banks operate and hence the way that they can do business. Those Chicago banks that are members of the Federal Reserve System must comply with the System's requirements about reserves, maximum interest rates payable on deposits, and so on; and in addition, of

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[6] Statement by the EC, ECB and IMF on the Third Review Mission to Greece (Feb. 24, 2011).

[7] *See, e.g.*, IMF Staff Report, Ireland: Extended Arrangement—Interim Review Under the Emergency Financing Mechanism (Feb. 2011) at http://www.imf.org/external/pubs/ft/scr/2011/cr1147.pdf .

[8] Strengthening Economic Governance in the EU Report of the Task Force to the European Council, 3 (Oct. 21, 2010) at http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/117236.pdf.

course, with the requirements of the Comptroller of the Currency if they are national banks, and of the Illinois State Banking Commission if they are state banks.

Euro-dollar banks are subject to the regulations of the relevant banking authorities in the country in which they operate. In practice, however, such banks have been subject neither to required reserves on Euro-dollar deposits nor to maximum ceilings on the rates of interest they are permitted to pay on such deposits.

The difference in regulation has played a key role in the development of the Euro-dollar market. No doubt there were minor precursors, but the initial substantial Euro-dollar deposits in the post-World War II period originated with the Russians, who wanted dollar balances but recalled that their dollar holdings in the U.S. had been impounded by the Alien Property Custodian in World War II. Hence they wanted dollar claims not subject to U.S. governmental control.

The most important regulation that has stimulated the development of the Euro-dollar market has been Regulation Q, under which the Federal Reserve has fixed maximum interest rates that member banks could pay on time deposits. Whenever these ceilings became effective, Euro-dollar deposits, paying a higher interest rate, became more attractive than U.S. deposits, and the Euro-dollar market expanded.

A third major force has been the direct and indirect exchange controls imposed by the U.S. for “balance-of-payments” purposes - the interest-equalization tax, the “voluntary” controls on bank lending abroad and on foreign investment, and, finally, the compulsory controls instituted by President Johnson in January 1968.[9]

An article in the BIS Quarterly Bulletin for September 2004[10] says:

The geopolitical environment during the cold war and the regulation of US domestic banks in the 1960s and 1970s led oil-producing countries to search for a home outside the United States for their US dollar deposits. A long history as a global trade centre, coupled with a loosening of regulations on offshore transactions in the late 1950s, allowed London to emerge as the repository for these dollars. Over the past 30 years, US dollar deposits outside the United States, or “eurodollars”, have grown exponentially, with London remaining at the centre of this market.

This growth in eurodollar deposits has been a function of the greater efficiency of eurobanks relative to banks in the United States. Because eurobanks face fewer regulations than their

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[9] Milton Friedman, The Eurodollar Market: Some First Principles, Selected papers No. 34, Graduate School of Business, University of Chicago, *available at* http://www.chicagogsb.edu/faculty/selectedpapers/sp34.pdf .

[10] http://www.bis.org/publ/qtrpdf/r_qt0409g.pdf

domestic counterparts (eg reserve requirements), they can operate at lower spreads and hence offer more competitive deposit and loan interest rates. With these lower operating costs, eurobanks have been able to attract deposits that would otherwise be placed in US domestic banks. As a result, the eurodollar market serves as an arena for the global recycling of funds, whereby eurobanks not only manage their own US dollar positions vis-à-vis other currencies, but ultimately place them in the hands of the global borrowers best able to use them.

The BIS noted a decline in the recycling rate of eurodollars in London - rather than remaining in the interbank market in London eurodollars were being lent to non-bank borrowers, mainly in the US.[11]

In the past Libor was not one fixed rate of interest, but could vary to reflect the different costs which different banks might incur in borrowing money in the interbank market. Loan agreements used to specify a process for calculating Libor for a particular loan, which would involve specifying which banks would be involved in quoting rates for Libor for different interest periods under the loan. Libor is supposed to reflect the lenders' cost of funds (the borrower under the loan agreement will pay Libor plus a margin where the margin is the lenders' profit on the loan). The use of Libor assumes that the lending banks will be funding their loan commitments from the interbank market rather than from deposits. Thus it is important that the rate quoted actually reflects the lenders' cost of funds. It is worth noting that the rates at which banks actually lend money to each other during any day will vary.

A bank which seeks to borrow money in the interbank market will need to pay a level of interest which reflects both prevailing market conditions and the lender's assessment of the borrowing bank's financial condition. Weaker banks would expect to pay higher interest rates. So a weak bank lender under a loan agreement which relied on strong banks to set Libor could find that the loan was unprofitable for it.

Libor is now a standardised rate of interest as the British Bankers' Association (BBA) developed a mechanism for fixing Libor for different currencies, and its rates are carried by various information providers.[12] You can find Libor (for US $) quoted in the

[11] Libor has become an alternative to Prime Rate, which is the interest rate banks charge for short-term loans to their most creditworthy customers where there is little risk to the lender.

[12] *See* http://www.bbalibor.com/bba/jsp/polopoly.jsp?d=1621 .

financial pages of the newspapers,[13] and you can sign up for Libor tweets.[14] The agreement we are studying refers to Reuters as the source for the Eurodollar Base Rate.

The BBA relies on Contributor Panels, which are groups of banks who quote rates for different currencies. BBA identifies the banks which compose the contributor panels. In 2008 commentators began to criticise the arrangements for fixing BBA Libor, because, although it was clear that banks were reluctant to lend to each other, BBA Libor did not increase to reflect this fact.[15] People speculated that banks quoting as part of the BBA's contributor panels were unwilling to reveal through the quotes they submitted to the Libor fixing process that other banks had lost confidence in them and were raising the rates they were demanding to lend money. If contributor banks were submitting inaccurate quotes then Libor quoted by the BBA would also be inaccurate as a reflection of actual rates of interest lenders might be expected to pay. The BBA responded to these concerns by reviewing its procedures and by strengthening the governance arrangements for the Libor fixing process. A consultative paper published in June of 2008[16] was followed by a paper describing the new arrangements in November 2008.[17] The June paper described some of the issues as follows:

Transparency has long been one of the key attractions of LIBOR. Other indices either keep their contributors confidential (H15) or the bank is asked to contribute the rate at which it considers a hypothetical bank would borrow (EURIBOR). LIBOR contributors on the other hand provide the rate at which they believe they could borrow should they propose so to do. The issue has been raised as to whether this has the potential to stigmatise contributions and therefore the BBA proposes to explore options for avoiding any stigma whilst maintaining

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[13] Libor has been used as the basis for the interest rate in adjustable rate mortgages in the US domestic market.

[14] *See* BBA LIBOR: the world's most important number now tweets daily (May 21, 2009) at http://www.bbalibor.com/news-releases/bba-libor-the-worlds-most-important-number-now-tweets-daily.

[15] *See, e.g.*, http://uk.reuters.com/article/businessNews/idUKL2984225820080529?sp=true.

[16] BBA, Understanding the Construction and Operation of BBA LIBOR - Strengthening for the Future (Jun. 10, 2008) available at http://www.aciforex.org/docs/markettopics/20080610__BBA_comments_on_Libor_fixing.pdf.

[17] See BBA, LIBOR Governance and Scrutiny - Proposals agreed by the FX & MM Committee (Nov. 17, 2008) *available from* http://www.bbalibor.com/news-releases/libor-gets-enhanced-governance-and-scrutiny-procedures .

transparency...
BBA LIBOR is by far the most widely referenced interest rate index in the world. Its importance goes beyond that of inter bank lending and touches everyone from large international conglomerates to small borrowers. It is central in interest rate swaps and the great majority of floating rate securities and loans relate to LIBOR. Independent research indicates that around $350 trillion of swaps and $10 trillion of loans are indexed to BBA LIBOR. It is the basis for settlement of interest rate contracts on the world's major futures and options exchanges. It is written into standard derivative and loan documentation such as the ISDA terms and is also used for an increasing range of retail products...
LIBOR is owned by the BBA which is a not for profit organisation funded primarily by subscriptions from its voluntary members. The data for the LIBOR fixes is compiled and calculated by Reuters for the BBA. The contributing banks for each LIBOR currency are selected on objective criteria and may or may not be members of the BBA. Those who are members they pay an annual standard subscription to the Association. There is no levy charged for any bank which contributes to or participates in the LIBOR fix...
LIBOR has an unbroken back-history stretching back to 1985 and it has enjoyed an enviable reputation since its inception.[18]

The new arrangements involve a committee, the Foreign Exchange and Money Markets Committee (FX & MM Committee), with sub-committees, one of which is responsible for fixing Libor, another which is responsible for oversight, and a third which is a steering group responsible for reviewing membership of the panels. There are new disciplinary procedures. In contrast to past practice the names of the firms which are represented on the committee are disclosed, and the firms are chosen to reflect a range of different interests:

Currently Committee members sit in their own right as individuals, and membership is not publicly disclosed. However there is justifiable interest from the market in the make-up of the Committee, as they wish to see that the body is independent and appropriately constituted...
In future, therefore, committee members will sit as individuals representing their firms, and will be expected to act in the best interests of the LIBOR benchmark and the markets it serves. The committee will be expanded to include:
A representative of a (currently) non-contributing US bank that is active in the money markets
A representative of a (currently) non-contributing European bank that is active in the money

[18] The paper explains that "H15 is the yield in the three month Euro Dollar deposit rate published daily by the Fed. The Fed's measure of USD Euro Dollar rates is based on the yield observed within the Euro Dollar deposit market and the H15 values had tended to be at the high end of the traded range."

markets
One representative from Liffe and one from the Chicago Mercantile Exchange (CME)
Two “rate takers”: one from the fund management industry and one from the Association of Corporate Treasurers...
The BBA will contact the above and present a list of names and titles for consideration by the Committee...
Once the Committee has reached its complement, the names of all firms represented will be released, but not names of the individual members. This will be accompanied by a statement which describes the capacity in which members serve...
The BBA is subject to a regular independent audit of practices and processes and in future the FX & MM Committee and LIBOR processes will be included in this audit.[19]

These changes to the governance arrangements for the Libor fixing process are similar to recent changes to exchange governance arrangements (in the inclusion of representation of a wider range of interests).

For the euro there is an interest rate called Euribor (Euro Interbank Offered Rate) which is “the rate at which euro interbank term deposits within the euro zone are offered by one prime bank to another”,”[20] and, like BBA Libor, is fixed by a panel of banks. The Euribor Code of Conduct specifies the rules that apply to Euribor and panel banks.[21]

Consider how the agreement addresses issues associated with reliance on funding in the interbank market (section 3.03, the definition of Eurodollar Base Rate).

CONTRACTS AND UNCERTAINTY: DEFAULT INTEREST, FREEZES

Loan Agreements typically apply a higher rate of interest to borrowers after any default in payment. For a case stating that a 1% default interest provision did not constitute a penalty because it was a modest increase and reflected the increased risk for the lenders after a default by a borrower see **Lordsvale Finance plc v Bank of**

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[19] LIBOR Governance and Scrutiny at p. 6.

[20] http://www.euribor.org/

[21] It can be found at http://www.euribor-ebf.eu/assets/files/Euribor_code_conduct.pdf.

Zambia [1996] 3 All ER 156 (QBD, Colman J.)[22]:

... Where, however, the loan agreement provides that the rate of interest will only increase prospectively from the time of default in payment, a rather different picture emerges. The additional amount payable is ex hypothesi directly proportional to the period of time during which the default in payment continues. Moreover, the borrower in default is not the same credit risk as the prospective borrower with whom the loan agreement was first negotiated. Merely for the pre-existing rate of interest to continue to accrue on the outstanding amount of the debt would not reflect the fact that the borrower no longer has a clean record. Given that money is more expensive for a less good credit risk than for a good credit risk, there would in principle seem to be no reason to deduce that a small rateable increase in interest charged prospectively upon default would have the dominant purpose of deterring default. That is not because there is in any real sense a genuine pre-estimate of loss, but because there is a good commercial reason for deducing that deterrence of breach is not the dominant contractual purpose of the term.

It is perfectly true that for upwards of a century the courts have been at pains to define penalties by means of distinguishing them from liquidated damages clauses. The question that has always had to be addressed is, therefore, whether the alleged penalty clause can pass master as a genuine pre-estimate of loss. That is because the payment of liquidated damages is the most prevalent purpose for which an additional payment on breach might be required under a contract.

However, the jurisdiction in relation to penalty clauses is concerned not primarily with the enforcement of inoffensive liquidated damages clauses, but rather with protection against the effect of penalty clauses. There would therefore seem to be no reason in principle why a contractual provision, the effect of which was to increase the consideration payable under an

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[22] Compare, e.g., *Norwest Bank Minn., N.A. v. Blair Rd. Assocs., L.P.*, 252 F. Supp. 2d 86 (District of New Jersey 2003) (rejecting argument that a default interest provision was a penalty: “Where enforceable, a stipulated damages clause is referred to as liquidated damages... Nevertheless such a clause requires judicial scrutiny because it may constitute an oppressive penalty and hence be unenforceable...a default interest rate, like late fees, is subject to the test of reasonableness.”); cf. *Cantamar, L.L.C. v. Champagne*, 2006 UT App 321 (“We conclude the 30% per annum default interest rate agreed to by DSI under the terms of the Note is not substantively unconscionable. In light of DSI's execution of prior notes with previous lending companies, DSI was not an inexperienced party to such agreements... and cannot claim surprise, particularly where the default interest rate under the Note was lower than the interest rates of the two prior notes the Note refinanced. Additionally, because the Note constituted a refinancing of DSI's prior obligations under two earlier promissory notes to a different lender, including unpaid interest and fees, Cantamar assumed more than a minimal amount of risk in refinancing DSI's earlier loans. Even presuming the Note's default was "high by some standards," the Utah Supreme Court has previously explained that "[a]cquisition of high risk capital almost always requires the payment of a premium," and thus "[i]t is not sound legal policy to establish rules so strict as to unnecessarily dampen legitimate and desirable business activity.")

executory contract upon the happening of a default, should be struck down as a penalty if the increase could in the circumstances be explained as commercially justifiable, provided always that its dominant purpose was not to deter the other party from breach.

In **Murray v Leisureplay plc** (2005)[23] the English Court of Appeal had to consider the question whether a contractual provision for damages in an employment contract functioned as a penalty. Lady Justice Arden said:

29 The penalty issue is one of considerable jurisprudential interest. English law is well-known for the respect which it gives to the sanctity of contact. The question which the law of penalties poses is this: to what extent does English contract law allow parties to a contract to specify for their own remedies in damages in the event of breach? The answer is that English law does not in this particular field take the same laissez-faire approach that it takes to (for example) the question whether parties can agree to time limits for the performance of obligations which they subsequently find difficulty in meeting. So far as that is concerned, pacta sunt servanda. So far as pre-determined damages clauses are concerned, English contract law recognises that, if the parties agree that a party in breach of contract shall pay an unjustifiable amount in the event of a breach of contract, their agreement is to that extent unenforceable . The reasons for this exception may be pragmatic rather [than] principled....
43 The usual way of expressing the conclusion that a contractual provision does not impose a penalty is by stating that the provision for the payment of money in the event of breach was a genuine pre-estimate by the parties to the agreement of the damage the innocent party would suffer in the event of breach. As Lord Dunedin said in the Dunlop case, the "essence" of a liquidated damages clause is "a genuine covenanted pre-estimate of damage" ... As the Dunlop case and the citation from the Philips case... show, a contractual provision does not become a penalty simply because the clause in question results in overpayment in particular circumstances. The parties are allowed a generous margin..
54 With the benefit of the citation of authority given above, in my judgment, the following (with the explanation given below) constitutes a practical step by step guide as to the questions which the court should ask in a case like this:-
i) To what breaches of contract does the contractual damages provision apply?
ii) What amount is payable on breach under that clause in the parties' agreement?
iii) What amount would be payable if a claim for damages for breach of contract was brought under common law?
iv) What were the parties' reasons for agreeing for the relevant clause?
v) Has the party who seeks to establish that the clause is a penalty shown that the amount

[23] [2005] EWCA Civ 963 at http://www.bailii.org/ew/cases/EWCA/Civ/2005/963.html

payable under the clause was imposed in terrorem, or that it does not constitute a genuine pre-estimate of loss for the purposes of the Dunlop case, and, if he has shown the latter, is there some other reason which justifies the discrepancy between i) and ii) above?
55.... the test of genuineness is objective. A pre-estimate is genuine if it is not unreasonable in all the circumstances of the case.

The other two judges in the case took what they described as a broader view in which they approved of the approach of Colman J. in the Lordsvale Finance case and also suggested that courts should be more reticent about invalidating contractual provisions than Lady Arden's judgment suggested. For example, Lord Justice Buxton said:

116 It is therefore necessary to stand back and look at the reality of this agreement. Although I agree that evidence about it is sparse, I am prepared to take judicial notice of the fact that an entrepreneurial company such as MFC, promoting a product conceived by one man, will often place a high value upon retaining the services, and the loyalty and attention, of that one man as its chief executive: to the extent of including in his "package" generous reassurance against the eventuality of dismissal. That such reassurance exceeds the likely amount of contractual damages on dismissal does not render the terms penal unless the party seeking to avoid the terms can demonstrate that they meet the test of extravagance posited by Lord Dunedin and by Lord Woolf. I regard that as a comparatively broad and simple question, that will not normally call for detailed analysis of the contractual background. Applying that test, which I accept differs from that adopted by my Lady, I would accordingly allow the appeal on the penalty issue.
117 I would add this. The difficulty that the court has in identifying a penalty in an orthodox commercial contract is demonstrated by the outcome of the Dunlop case itself. The clause in question was a standard form, imposed on all of Dunlop's customers, that required the payment of five pounds by way of "liquidated damages" if the customer did any one of the acts of tampering with marks on the goods; selling at under list price; supplying to persons blacklisted by Dunlop; or exporting without Dunlop's consent. Contrary to what would be thought today, the House did not view the fact that the clause was part of a contract of adhesion as undermining its status as an agreement freely bargained for... The clause imposed a single payment for any of a varied series of breaches; but assisted by Dunlop's evidence as to the benefits to the company of the price maintenance policy (expressly so described) that the clause imposed, as set out in particular by Lord Atkinson in both the Dunlop cases, the House concluded that an explanation of the clause in commercial rather than deterrent terms was available. That commercial explanation lay in Dunlop's desire enforce its commercial policy without the difficulty and burden of proving the quantum of damage accruing from every particular breach of that policy.

118 Dunlop differed from the present case in that the House was impressed by the difficulty of proving an exact loss in every, or any, of the many cases of breach to which the clause extended. That particular problem does not affect our case. But the cautious approach of the House, and its willingness to look at the clause in its commercial context, does at least underline the importance stressed by Lord Woolf of not moving automatically from the fact that a clause could result in greater recovery than the amount of the actual loss to an assumption that without further justification the clause must be penal in nature.

The issue of penalties arose in December 2009 in litigation involving currency swaps under an ISDA Master Agreement in **BNP Paribas v Wockhardt EU Operations (Swiss) AG:**[24]

1 BNP Paribas, the claimant ("BNP"), has a branch in Mumbai. The defendant – Wockhardt EU Operations (Swiss) AG ("Wockhardt") – is a Swiss company and a wholly owned subsidiary of Wockhardt Ltd, an Indian company, based in Mumbai. Wockhardt Ltd is a leading pharmaceutical and biotechnology company – the largest Indian pharmaceutical group in Europe. BNP has an established banking relationship with Wockhardt Ltd.
2 In April 2008 BNP and Wockhardt entered into a Master Agreement in the standard form of the International Swap Dealers Association (ISDA)... A number of transactions were entered into pursuant thereto. Those transactions fall, so far as presently relevant, into two categories.
3 In the first category were foreign exchange target redemption forward transactions. By these transactions, so far as presently relevant, BNP sold euros to Wockhardt for dollars. In the second category were a number of foreign exchange forward transactions. These were transactions under which Wockhardt agreed to buy from BNP on a series of settlement dates an amount of either Euros or dollars (the amount being established by reference to a notional amount in Euros) for dollars or euros as the case might be at a defined rate of exchange....
10. .. BNP provided to Wockhardt a Statement of Calculations pursuant to clause 6(d)(i) of the Master Agreement, showing the Early Termination Amount payable by Wockhardt ("the Early Termination Amount"), which then stood at US$2,150,570.10. To that sum was added default interest which had accrued from 2 April to 22 April 2009 in the sum of US$1,503.06. The total sum of US$2,152,073.16 was due and payable immediately.
11. The Early Termination Amount claimed by BNP was, apart from interest, made up of two elements:

(a) unpaid amounts already due under specific forward deals amounting (as at 22 April 2009) to US$1,260,090 ("the Unpaid Amounts") and

(b) a Close-out Amount of US$890,480 ("the Close-out Amount")....

[24] [2009] EWHC 3116 (Comm) at http://www.bailii.org/ew/cases/EWHC/Comm/2009/3116.html

22. Mr Antony White QC on behalf of Wockhardt submits that it has an arguable case that the provisions relating to an Early Termination Amount are unenforceable by reason of the doctrine relating to penalties. The Early Termination Amount is a sum payable upon breach following the giving of a Notice of Default and a failure to pay within a very short period after notice of an earlier failure. The full Early Termination Amount is payable (i) whether the defaulting party has one open transaction or many open transactions; (ii) whether the default occurs early in the life of a Transaction or towards the end of its life; (iii) whether the default is a small default on one Transaction, a large default on one Transaction or a large default on many or all Transactions; and (iv) the amount of the Early Termination Amount cannot be predicted at the time of entering into the Transactions as it depends on upon market fluctuations. For all these reasons the provisions providing for an Early Termination Amount, at any rate in relation to the Close-out Amount are penal. They do not provide for a genuine pre-estimate of the loss but for payment of the same amount on the occurrence of any one of a number of possible breaches which may give rise to widely different consequences. At any rate there is a realistic argument that that is so

23 In considering the potential application of the doctrine of penalties the authorities provide a number of guidelines. The ISDA Master Agreement is very widely used in international financial markets in all types of derivative transactions. That does not mean that its standard provisions may not be penal but the consequences of that being so means that the sooner the issue of its validity is determined the better...

24 The desirability of a prompt determination cannot alter the test as to whether some form of summary judgment should be given, but:

".. on general principles the court should not be astute to interpret commercial transactions so as to invalidate them, particularly when . consequential doubt might be cast on other long-standing commercial arrangements": Perpetual Trustee Co Ltd v BNY Corporate Trustees Services and another; Belmont Park Investments Pty Ltd v Corporate Trustee Services Ltd and another [2009] EWHC 1912 (Ch) per Sir Andrew Morritt, QC.

"It is also desirable that, if possible, the courts give effect to contractual terms which the parties have agreed. Indeed there is a particularly strong case for party autonomy in cases of complex financial instruments ." per the Master of the Rolls at para 58 of the Butters appeal [2009] EWCA Civ 1160.

".the power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression"; per Dickson J in the Supreme Court of Canada in Elsey v J.G. Collins Insurance Agencies Ltd [1978] 83 DLR 1, p 15. , approved by the Privy Council in Phillips Hong Kong Ltd v AG of Hong Kong [1993] 61 BLR 49, p 58.

25 The policy of the law is to encourage the use of liquidated damages clauses especially in commercial contracts: Murray v Leisureplay plc [2005] EWCA Civ 963, para 114 citing Diplock,

LJ in Robophone v Blank [1966] 1 WLR 1428, 1447.

26 Lord Dunedin classically described a penalty clause as one which stipulates a pre-defined sum payable on one or more breaches of contract "if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach": Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd [1915] AC 79, 87. In the same case he said that there was a presumption (but no more) that a clause is a penalty when 'a single lump sum is made payable by way of compensation on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage". In such a case the court may look to see whether or not the sum is disproportionate to the least important of the contractual undertakings to which it applies and thus whether it represents an extravagant or unconscionable sum in relation to such a breach.

27 In the present case the clause pre-defines not the sum, but the method by which a sum - the Early Termination Amount, is to be determined and by whom. The fact that it prescribes a method would not save it from being a penalty if the result of the application of the method was to produce an amount which was extravagant and unconscionable in the respects described by Lord Dunedin. The fact that it does not contain a pre-estimate in the sense of a fixed figure or one easily determinable by a specified formula (as opposed to a criterion) does not mean that it must, on that account, be penal.

28 In order to determine whether the clause is penal in consequence it is necessary to consider what is due to BNP following termination in consequence of the breach.

29 So far as the Unpaid Amounts are concerned, they had already fallen due before termination under individual forward transactions. There is nothing penal in requiring Wockhardt, the defaulting party, upon a termination following an Event of Default, to pay amounts that were already due but unpaid prior to the termination.

30 So far as the Close-out Amount is concerned the critical question, to my mind, is whether or not non-payment of any amount due on delivery amounts to a breach of condition by virtue of which BNP is entitled to treat itself as discharged from its obligations under the contract and entitled to damages for the loss of its bargain upon the footing that the contract has come to an end by virtue of Wockhardt's default.

31 Mr White submits that that is not, or at least arguably is not, the position here since the parties have not specified that punctual payment of each amount due was a condition, or non-payment a repudiatory breach, and there is no need for that to be implied.

32 I disagree. Whilst the parties have not used the expression "condition" or "repudiatory breach" they have specified that any failure to pay which continues after the first Local Business Day after notice of failure will entitle BNP to designate an Early Termination Date; and have gone on to provide that upon an effective designation no further payments or deliveries (the primary obligations under the contract) will be due. Wockhardt's obligation to make future payments against deliveries will, therefore, cease as will BNP's obligations to make deliveries

against payment. In the place of those obligations there is to be substituted an obligation on the part of Wockhardt, the defaulting party, to make a payment which represents the cost of replacing the Terminated Transactions or in providing the economic equivalent of those Transactions. The former would, no doubt, need to take into account any price to be paid for replacing the terminated transactions as at the Early Termination Date. The latter would involve a determination of the value as at the Early Termination Date of the remainder of the contract i.e. the present value, allowing for the time value of money, of putting BNP into the same position as it would have been in if the uncompleted sales of euros had gone ahead according to their terms. These are two methods of putting BNP into the same position it would have been if the contract had not been validly terminated on account of Wockhardt's breach. Neither of them provides for an extravagant or unconscionable measure if what is being measured is BNP's loss of bargain.

33 In providing for BNP's entitlement to terminate the ongoing primary obligations of the parties and the method of calculation of the sum to be paid in that event, the parties have, subject to one qualification, spelt out the consequences which result from a breach of condition. It is unrealistic to suppose that, having done so, they are to be taken to have intended that a failure to pay should be regarded as a warranty or an innominate term, particularly in the light of the Pre - Estimate clause which (see above) provides that the amount recoverable under clause 6 (e) is payable for the non Defaulting Party's loss of bargain and the loss of protection against future risks. Commercial parties to a contract for the sale and delivery of currency who specify that non-payment or non-delivery shall have the consequences which would follow from a breach of condition, both as to entitlement to terminate and measure of recovery, must be taken to have agreed that the term in question shall have that status. The expressions "condition" and "repudiatory breach" are legal shorthand for a term breach of which entitles the innocent party to terminate the contract and to claim damages for loss of bargain or a breach which has those consequences. When the parties have expressed those consequences for themselves they have no need of the shorthand.

34 Whilst by section 41 of the Law of Property Act 1925 stipulations as to time which "according to rules of equity are not deemed to be or to have become of the essence of the contract are also construed and have effect at law in accordance with the same rules" time is held in equity to be of the essence of the contract "in cases of direct stipulation or of necessary implication": per Sir John Romilly M.R in Parkin v Thorold [1852] 16 Beav 59, 65; and that implication can arise from the nature and content of the contract.

35 Mr White submitted that to hold that the doctrine of penalties was not applicable because the contract specified the consequences of breach was to misunderstand the rule. Where the doctrine is applicable it takes effect notwithstanding that the contract provides for the payment in question. That does not, however, mean that the court is disabled from construing the nature of the obligation which the parties have agreed on from an examination of (i) the obligation in question (here payment against delivery) and (ii) the consequences which the parties have

agreed shall follow on fulfilment (termination at the option of BNP and compensation for loss of bargain).

36 A clause prescribing the damages payable upon breach could still be a penalty if it prescribed an extravagant payment even for a breach of condition: see Lombard PLC v Butterworth [1987] QB 527, 535, proposition 7. The present clause does not, however, do so.

37 The qualification is that the Early Termination Sum is a calculation of the net position between the parties as at the date of termination in relation to Terminated Transactions. The defaulting party will thus, in any event, be entitled to credit for any positive present value in its favour in respect of those transactions. The valuation does not necessarily result in sums becoming payable from the defaulter to non-defaulter; they can be payable in either direction. No doubt BNP will not be inclined to terminate the agreement if, upon its so doing, it would not receive any sum, unless, perhaps, it thought that a later termination might put it in a position where it would have to pay out even more. What it cannot, however, do is to refuse to credit Wockhardt with any overall net balance in its favour upon the ground that it was discharged from all future performance. Since that is something which redounds to Wockhardt's advantage it cannot be relied on as making the provisions penal.

38 The effect of the provisions is not that either party receives a windfall but that both receive the benefit (or disbenefit) of the unperformed transactions comprising their agreement crystallized at an earlier point in time (of the Non Defaulting party's choosing). Whilst the analogy is not exact, since the amount, if any, payable as an Early Termination Amount (and thus the total value of the performance remaining) will change throughout the life of the agreement in line with market fluctuations, there is nothing penal in a provision which requires the acceleration in the event of breach of an amount which, without breach, would become due later: Protector Endowment Loan Co v Grice (1880) 5 QBD 592; The Angelic Star [1988] I Lloyd's Rep 122, 125-7.

39 The clause does not become unconscionable or extravagant simply because it provides for a determination of what is to be due to be made by the Non Defaulting party, particularly when it requires BNP to "act in good faith and use commercially reasonable procedures in order to produce a commercially reasonable result."...

44 Mr White submitted that in the present case there were two indicators of the penal nature of the provisions which required the Court to consider their commercial justification e.g., by considering their genesis, the nature of the negotiations or considerations that had led to them, and the problems, if any, which they were designed to address. Such a consideration was inappropriate for a summary process; and, indeed, there was very little evidence of the reasonableness of the provision. The first indicator was that the same sanction – the close out of the Transactions – was exigible for breaches of very different seriousness. The second was that the clause provided for the payment of a fluctuating amount since the sum to be paid would alter according to market rates or volatility, matters which were extraneous to the breach.

45 I do not accept this submission. The fact that the clause is capable of application to several

breaches of different seriousness might well be an indicator that it was penal in character but for the fact that, in my judgment, the provision of timely payment is a condition of the agreement. The fact that the amount to be paid will fluctuate according to the movements of the market is not something extraneous to the breach. It is a circumstance that must necessarily be taken into account in determining the present value of the contract at any given time.

46 Reliance was placed on the decision in Public Works Commissioner v Hills [1906] 1 AC 368 where a railway construction contract provided that in the event of a breach by the contractor he should forfeit "as and for liquidated damages" certain percentages retained by the Government of the Cape of Good Hope of money payable for work done as a guarantee fund to answer for defective work and also certain security money deposited with the Government. The amount of that retained money depended on the progress of contracts other than the one in suit. That was an example of a liquidated damages clause whose operation was dependent on facts which had nothing to do with the relevant breaches. But that is a circumstance far removed from this case.

47 I was also referred to the observations of Thomas, LJ at paragraph 49 in Cine Bes Filmcilik Ve Yapimcilik & Anr v United International Pictures & Ors [2003] EWCA Civ 1669 that "a decision on whether [a clause] is penal involves a careful examination of the circumstances which is not possible on a Part 24 application". I do not, however, understand him to have laid down that a summary decision in relation to whether a clause is penal is always inappropriate. In that particular case the clause failed to give credit for rights to films for which payment would have been made against sums payable on termination; and that was regarded as a circumstance which required justification or, at least an examination as to whether or not its effect was penal. That feature does not arise here.

48 Mr White directed my attention to a passage in The Law on Financial Derivatives, 4th edition para 3.11 where Professor Hudson refers to the "artificial link" between the transactions constituted by the provision in the Master Agreement that all of the Confirmations entered into between two parties together with their Master Agreement, Schedule and Credit Support documentation are construed as constituting one single contract. The reason, as he points out, for introducing this artificial link is so as to secure that on the termination of the relationship between the parties it is possible to set off all of the amounts owed between the parties and to come to one final, net sum which will settle all of the exposures of the parties one to another, a provision which may assume very great importance upon insolvency. The link is designed to avert the risk that the solvent party may be required to make payment of all amounts which it owes but not be entitled to recover, save through the relevant insolvency process and to the extent that there is a sufficiency of assets, the amounts due to it.

49 The fact is, however, that the parties have created that link by their agreement, as they were entitled to do. Their intention, as manifested in the language which they have used, is that the Master Agreement and all Confirmations shall form a single agreement between the parties, and that prompt payment in respect of each individual transaction shall be an essential term of

that agreement. There is, in my judgment, no reason why a commercial contract such as this should not take effect in accordance with its terms; nor anything particularly surprising in a provision which makes payment of the debt within a day of notice of failure a condition. Mr White submitted that, if the link between transactions was artificial, the doctrine of penalties was engaged because that doctrine was concerned with substance. But, in truth, there is nothing artificial about the agreement of the parties. They have by agreement produced a situation which, in the absence of their agreement, would not have arisen; but their agreement prescribes the substance of the legal relations into which they have freely chosen to enter.

50 In short there is, in my judgment, no realistic prospect of Wockhardt establishing that the Early Termination provisions are penal in character. I note that in the New York case of Drexel Burnham Lambert Products Corporation v Midland Bank PLC 92 Civ 3098 (MP) the US District Court for the Southern District of New York held, on a motion for summary judgement, that a "Limited Two-Way Payments Clause" contained in a Swap Agreement constituted a valid liquidated damages clause and was enforceable in accordance with its terms since it bore a reasonable relationship to the probable loss. I do not, however, base my decision on that case in any way since both the terms of the clause and the applicable law are unclear....

These cases seem to suggest that courts in England are prepared to review the details of commercial contracts to determine whether or not provisions for payment in certain circumstances constitute penalties (the penalties argument here is not dismissed out of hand but seems to be considered seriously). Do you think that this is appropriate? This last case arose in the context of a standard form document developed by ISDA and used in numerous financial transactions. Do you think that a commonly used form of document should be treated with greater care (on the grounds of legal certainty) by a judge than a less commonly used form? Does/should it make a difference to a judge in one jurisdiction that a contractual term in a standard form document used around the world is treated as valid in other jurisdictions? Do you think it would be useful to be able to develop a system for evaluating the legal effectiveness of such documents in advance?

The risk that a contract will not be enforced by courts in the way that parties to the contract intend is an aspect of legal risk (which also includes the risk that statutes and regulations may be interpreted in surprising ways). Legal risk also includes risks associated with changes in circumstances, such as bankruptcy, as bankruptcy laws change the legal rights of parties to contracts.

The following case arises out of a US freeze on payments to Libya. It illustrates some of the uncertainties which may impact international financial transactions and which banks have to be aware of and plan for. It also examines choice of law issues in the context of

the eurodollar, and allows us to think about some payment systems issues. What does Staughton say was the proper law ? Do you agree with him? Do you agree with his reactions to the testimony of the expert witnesses?

Libyan Arab Foreign Bank v Bankers Trust (Staughton J)[25]

The plaintiffs are a Libyan corporation, wholly owned by the Central Bank of Libya. They carry on what is described as an offshore banking business, in the sense that they do not engage in domestic banking within Libya. I shall call them "the Libyan Bank." The defendants are a New York corporation with their head office there. They no doubt have a number of branches in various parts of the world; but I am concerned with one in particular, their branch in London. I shall refer to them as "Bankers Trust," and when it is necessary to refer to particular offices as "Bankers Trust London" or "Bankers Trust New York."

In January 1986 the Libyan Bank had an account with Bankers Trust London, denominated in United States dollars. That was a call account, which meant that no cheque book was provided, interest was payable on the balance standing to the credit of the account at rates which varied from time to time, and some minimal period of notice might be required before instructions relating to the account had to be complied with. The suggestion in this case is that instructions would have to be given before noon if they were to be carried out that day. In English practice it would, I think be described as a species of deposit account. The amount standing to the credit of that account at the close of business on 8 January 1986 was U.S.$131,506,389.93. There may be a small element of subsequent adjustment in that figure. But the point is not material.

The Libyan Bank also had an account with Bankers Trust New York, again denominated in United States dollars. This was a demand account. No interest was paid on the balance, and no significant period of notice was required before instructions had to be complied with. But there was not, so far as I am aware, a cheque book. In England it would have been a current account. The amount standing to the credit of that account at the close of business on 8 January 1986 was U.S.$251,129,084.53.

Relations between Libya and the United States in January 1986 were not good. At 8.06 p.m. New York time on 7 January the President of the United States of America issued an executive order, which had the force of law with immediate effect. It provided, so far as material:

"Section 1. The following are prohibited, except to the extent provided in regulations which may hereafter be issued pursuant to this Order: ... (f) The grant or extension of credits or loans by any United States person to the Government of Libya, its instrumentalities and controlled

[25] [1989] Q B 728

entities."
That order did not in itself have any great effect on the events with which this case is concerned. But there followed it at 4.10 p.m. New York time on 8 January a second order, reading as follows:
"I, Ronald Reagan, President of the United States, hereby order blocked all property and interests in property of the Government of Libya, its agencies, instrumentalities and controlled entities and the Central Bank of Libya that are in the United States that hereafter come within the United States or that are or hereafter come within the possession or control of U.S. persons including overseas branches of U.S. persons. The Secretary of the Treasury, in consultation with the Secretary of State, is authorized to employ all powers granted to me by the International Emergency Economic Powers Act 50 U.S.C. 1701 et seq. to carry out the provisions of this Order. This Order is effective immediately and shall be transmitted to the Congress and published in the Federal Register.
Ronald Reagan
The White House
8 January 1986"

It is not in dispute that Bankers Trust are a United States person; or that Bankers Trust London are an overseas branch of a United States person; or that the Libyan Bank are an agency, instrumentality or controlled entity of the Government of Libya. Consequently by the law of and prevailing in the State of New York (which I shall refer to as New York law for the sake of brevity) it was illegal at and after 4.10 p.m. on 8 January 1986 for Bankers Trust to make any payment or transfer of funds to or to the order of the Libyan Bank in New York, either by way of debit to the Libyan Bank's account or as the grant of credit or a loan. Similarly it was illegal, by the law of New York or of any other American state, for Bankers Trust to make any such payment or transfer of funds in London or anywhere else.

The United Kingdom Parliament did not enact any similar legislation. No doubt there were reasons of high policy for that forbearance; but with them I am not concerned. It is sufficient to say that nothing in English domestic law prohibited such a transaction. So the main issues in this case are concerned with the rules of conflict of laws, which determine when and to what extent the law of New York is given effect in our courts, and with the contractual obligations of banks. In a word, Bankers Trust say that they cannot, or at any rate are not obliged to, transfer a sum as large as U.S.$100m. or more without using the payment machinery that is available in New York; consequently they have a defence to the Libyan Bank's claim, because performance of this contract would have required them to commit an illegal act in New York. Alternatively they say that their contract with the Libyan Bank is governed by the law of New York, so that performance is for the time being illegal by the proper law of the contract.

The Libyan Bank's claims

These are as follows (using a slightly different system of numbering from that adopted in the pleadings and in argument):

(1) The first claim is for the balance of U.S.$131,506,389.93 standing to the credit of the London account at the close of business on 8 January 1986. It is said that this sum is due to the Libyan Bank, and can be claimed on a cause of action in debt. Alternatively it is said that Bankers Trust ought to have responded to demands for U.S.$131m. that were made by the Libyan Bank in various different ways after 8 January, and are liable in damages.

(2) If they are right on the first claim, the Libyan Bank further say that one or other of three sums ought to have been transferred from the New York account to the London account on 7 and 8 January, thus increasing the amount which they are entitled to recover. These are: (i) U.S.$165,200,000 on 7 January, or (ii) U.S.$6,700,000 on 8 January, or (iii) U.S.$161,400,000 on 8 January. Indeed it is said that the sum of U.S.$6,700,000 was in fact transferred to London on 8 January, with the consequence that the Libyan Bank are in any event entitled to recover that additional amount.

(3) Largely but not entirely as an alternative to the second claim, the Libyan Bank say that they gave a number of payment instructions to Bankers Trust New York for execution on 8 January; those instructions could and should have been executed before 4.10 p.m. on that day, but were not. Consequently the Libyan Bank claim damages in the sum of U.S.$226,147,213.88.

(4) It is said that Bankers Trust, in breach of a duty of confidence which they owed to the Libyan Bank, disclosed information to the Federal Reserve Bank of New York on 7 or 8 January, and thereby caused damage to the Libyan Bank.

(5) Alternatively the Libyan Bank say that their contract with Bankers Trust has been frustrated, with the consequence that the Libyan Bank are entitled to the sums claimed under (1) and (2) above by virtue of the Law Reform (Frustrated Contracts) Act 1943 or as a restitutionary remedy at common law.

(6) Lastly there is a claim which is quite independent of the events of 7 and 8 January 1986 and President Reagan's executive orders. It is said that during the period from April 1984 to November 1985 Bankers Trust operated a system of transfers between the New York account and the London account, which was not in accordance with their contract with the Libyan Bank. In consequence the Libyan Bank were deprived of interest for one day or three days on a succession of sums during that period. It is said that the loss suffered is of the order of $2m. Bankers Trust do not deny that, initially, the system of transfers which they operated during this period failed to accord with their contract. But they say that, by the doctrine of account stated or estoppel, the Libyan Bank are precluded from asserting this claim.

The issues thus raised, or at any rate those that arise under paragraph (1) above, are of great interest and some difficulty. Similar problems occurred a few years ago in connection with the freeze on Iranian assets by executive order of 14 November 1979, and litigation was commenced. But before any of those actions could come to trial the freeze was lifted. This time

the problems have to be resolved.

History of the banking relationship
This can be considered in three stages. The first stage was from 1972 to 15 December 1980.

The Libyan Bank came into existence in June 1972. A correspondent relationship was established between the Libyan Bank and Bankers Trust. Initially an account was opened for that purpose with the Paris branch of Bankers Trust. But in April 1973 that account was closed, and an account opened with the London branch. It was described as a 7-day notice account. However, any requirement that notice of that length should be given before debits were allowed on the London account was not enforced. In this period the Libyan Bank did not wish to have any account with Bankers Trust New York. Transfers for the credit of the Libyan Bank used regularly to arrive at Bankers Trust New York, in accordance with the system most often used for transferring large dollar amounts, which I shall describe later. But they were dealt with by an instruction from Bankers Trust New York to Bankers Trust London to credit the account of the Libyan Bank there. Indeed the Libyan Bank insisted on that from time to time. Thus on 14 July 1973 they said in a telex to New York: "We also request immediate transfer of any funds you may receive in future for our favour to your London office." And on 17 July 1973 to London: "When we have agreed to have the account of Libyan Arab Foreign Bank with Bankers Trust I have made it very clear that no balance at all should be kept in New York and should be transferred immediately to our call account which started in Paris and now with you in London."

Certainly one motive for that attitude, and in 1973 possibly the only motive, was that dollar credit balances outside the United States earned a higher rate of interest than was obtainable in the United States. That is all that Eurodollars are - a credit in dollars outside the United States, whether in Europe or elsewhere. (It may be that one should add to this definition "at a bank" or "at an institution.") The interest rate is higher owing to the terms of the requirement imposed by the Federal Reserve Board that banks should maintain an amount equal to a proportion of the deposits they receive on deposit interest-free with the Federal Reserve system. That requirement is less demanding in connection with deposits received by overseas branches.

In fact Bankers Trust New York had operated an account in New York, for the handling of transactions by the Libyan Bank. But that account was closed on 17 December 1973 in consequence of the above and other protests by the Libyan Bank.

There followed a long period of discussion and negotiation. Bankers Trust were dissatisfied because the London, so-called 7-days' notice, account was used as a current account. Large numbers of transactions occurred on it, but interest was paid on the balance. This was not thought to be profitable for Bankers Trust. Furthermore, transfers to or from the account would commonly be made through New York, with a risk of delay and the possibility of error. On 23 November 1977 Mr. Ronai of Bankers Trust New York wrote to the Libyan Bank as follows:

"... I am writing to outline our proposal for clearing up the operational difficulties encountered in your dollar-clearing activity through Bankers Trust in New York.

"I feel that the problems stem from the number of intermediate steps required to effect a large number of transfers to and from your London Call account via New York. In order to simplify this situation, my proposal is to set up a fully-managed account relationship with Libyan Arab Foreign Bank. This should provide you with several major benefits, among which are:

- more timely information for yourselves
- simplification of transactions
- greater ease in researching possible errors
- the ability to tailor the system to your requirements.

"The basic elements of a managed account consist of a current account in New York and a call account in London with Bankers Trust Co. The current account will be used for your daily dollar-clearing activity; the call account should be considered as an investment of liquid funds. An explanation of the operation of your managed account follows.

"On a daily basis, all transactions concerning the demand account are reviewed, and the balance is 'managed' so that it does not exceed or fall below a predetermined target or 'peg' balance. Excess funds will be credited to your call account, or your current account will be funded from your call account, as the case may be."

In 1980 that proposal was more actively pursued. At first it was suggested by Bankers Trust that the current account should be in London. But by the time of a meeting in New York on 7 July it was again proposed that there should be a demand account there. Following that meeting Bankers Trust wrote from London to the Libyan Bank with details of the proposed managed account system:

"We will establish a 'peg' (or target) balance for the demand account of U.S.$750,000. That amount is intended to compensate Bankers Trust Co. for the services which we expect to provide, and is subject to periodic renegotiation as appropriate, for example when our costs increase, when interest rates decline significantly or when our level of servicing is materially changed. Each morning our account management team will review the demand account's closing book balance from the previous business day. If that balance is in excess of the 'peg,' they will transfer in multiples of U.S.$100,000 the excess amount to your call account in London with value the previous business day.

"Similarly, if the demand account balance is below the U.S.$750,000 peg, they will transfer funds back from your call account with value the previous business day. ... As you can appreciate, our account management team must closely follow the balance in your call account. Given time zone differences with London, all entries to your call account must be passed by that team in New York, and all your instructions to effect payments or foreign exchange settlements must be directed to our money transfer department in New York."

The figure of U.S.$750,000 as the peg balance was later agreed at U.S.$500,000.

There was some discussion of political risk at the New York meeting. I am confident that

political risk was at any rate in the minds of both parties, seeing that the freeze on Iranian assets had occurred only eight months previously. Mr. Abduljawad, then deputy chairman, is recorded as saying: "Placing at call is not an effort to avoid political risk, which he believes to be unavoidable." Whilst I accept that record as accurate, I also accept Mr. Abduljawad's oral evidence that "political risk is always being taken into consideration." Mr. Van Voorhees, who was among those attending the meeting on behalf of Bankers Trust, accepted that the Iranian crisis was at the back of everyone's mind in 1980.

A further meeting took place in Paris on 28 October 1980 between Mr. Abduljawad and Mr. Van Voorhees. At that meeting too no complete agreement was reached, so there was no new agreement or variation of the existing agreement. But important progress was made. Mr. Van Voorhees explained in plain terms that all the Libyan Bank's transactions would have to pass through New York. According to Mr. Van Voorhees, Mr. Abduljawad at first objected to that requirement, but later agreed to it. Mr. Abduljawad's evidence was that he did not reject it and equally did not agree to it. I do not need to resolve that conflict. It is plain to me that one of the terms which Bankers Trust were putting forward for the new arrangement was that all transactions should pass through New York; whether or not it was accepted at that stage is immaterial.

There followed a meeting in Tripoli and correspondence between the parties, and agreement was finally reached by 11 December 1980. Thus the managed account system was agreed on. Bankers Trust New York would open a demand account for the Libyan Bank, with a peg balance of U.S.$500,000. Transfers between that account and the call account in London would be made, as the need arose, in multiples of U.S.$100,000. The need for a transfer would be determined each morning by examining the closing balance of the New York account for the previous business day; if appropriate a transfer to or from London would be made with value the previous business day - in other words, it would take effect from that date for interest purposes.

It was, as I find, a term of that arrangement that all the Libyan Bank's transactions should pass through New York. Although not mentioned in the correspondence by which agreement was ultimately reached, this had plainly been a requirement of Bankers Trust throughout the later stages of the negotiations, and I conclude that it was tacitly accepted by the Libyan Bank. It was virtually an essential feature of the system: Bankers Trust New York would know about and rely on the credit balance in London in deciding what payments could be made from New York; they might be exposed to risk if the balance in London could be reduced without their knowledge. It was argued that such a term is not to be found in the pleadings of Bankers Trust; but in my judgment it is, in paragraph 3(4)(v) of the re-re-amended points of defence. There remains an important question whether the managed account arrangement was irrevocable, or whether it could be determined. I shall consider that later.

The second stage ran from December 1980 to November 1985. Before very long Bankers Trust took the view that the remuneration which they received from the relationship, in

the form of an interest-free balance of between U.S.$500,000 and U.S.$599,999 in New York, was insufficient reward for their services. On 15 March 1983 they proposed an increase in the peg balance to $1.5m. Negotiations continued for a time but without success. By 15 March 1984 Bankers Trust had formed the view that the Libyan Bank would not agree to an increase in the peg balance; so, on 3 April 1984, they decided unilaterally on a different method of increasing the profitability of the relationship for Bankers Trust; and it was put into effect on 17 April.

The new method required a consideration of the balance on the New York account at 2 p.m. each day. If it exceeded the peg balance of U.S.$500,000 the excess was transferred in multiples of U.S.$100,000 to the London account with value that day. Consideration was also given on the following morning to the balance at the close of the previous day. If it was less than the peg balance, a transfer of the appropriate amount was made from London to New York on the next day, with value the previous business day; if it was more than the peg balance there was, it seems, a transfer to London with value the same day. The effect of the change was that the Libyan Bank lost one day's interest whenever (i) credits received after 2 p.m. exceeded payments made after 2 p.m., and (ii) the closing balance for the day would under the existing arrangement have required a transfer (or a further transfer if one had been made at 2 p.m.) to be made with value that day. If a weekend intervened, three days interest might be lost. I am not altogether sure that I have stated the effect of the change correctly; but precision as to the details is not essential.

Bankers Trust did not tell the Libyan Bank about this change. Indeed an internal memorandum of Bankers Trust dated 14 August 1984 wondered whether Libya (possibly referring to the Libyan Bank) would notice the drop in interest earnings. Although the effect was on any view substantial, I am satisfied that the Libyan Bank did not in fact appreciate what was happening until mid-1985; and they complained about it to Bankers Trust in October 1985. I am also satisfied that the Libyan Bank could have detected, if they had looked at their statements from Bankers Trust with a fair degree of diligence, that they were not receiving the full benefit by way of interest to which they were entitled. Indeed, they did, as I have said, eventually detect that. But I am not convinced - if it matters - that they could have divined precisely what system Bankers Trust were now operating.

The third stage began on 27 November 1985, with a telex from Bankers Trust which recorded the agreement of the Libyan Bank to a new arrangement. This telex is important, and I must set out part of it:

"As discussed with you during our last meeting in your office in Tripoli, we have changed the method of investment from same day by means of next day back valuation, to actual same day with investment cut off time of 2 p.m. New York time. ... In this regard, those credits which are received after our 2 p.m. New York time cut off which result in excess balances are invested with next day value. This you will see from observing your account. For your information, the way our same day investment system works, is as follows: each day, at 2 p.m. the balance

position of your account is determined and any credits received up to that time, less payments and less the peg balance, are immediately invested. An example of this investment system can be seen for instance by comparing both statements of your demand and call accounts for 26 and 30 September 1985 which indicate same day investment on 26 September for U.S.$33.7 million which is reflected on your London call account statement on 27 September with value 26 September and on 30 September for U.S.$181.3 million which is reflected on your London call account statement on 1 October with value 30 September."

That was not in substance any different from the system which Bankers Trust had been operating since April 1984 without informing the Libyan Bank. It was now accepted by them.

7 and 8 January 1986

At 2 p.m. on 7 January the balance to the credit of the New York account was U.S. $165,728,000. (For present purposes I use figures rounded down to the nearest U.S.$1,000, save where greater accuracy is desirable.) Subject to two points which I shall consider later, a transfer of $165.2m. should then have been made to London. Mr. Fabien Arnell, an account manager of Bankers Trust New York, says somewhat laconically in his statement:

"On 7 January 1986 I instructed the managed account clerk not to make a 2 p.m. investment. I cannot now recall the precise reason why I gave that instruction."

During the rest of that day there were substantial transfers out of the New York account, with the result that it would have been overdrawn to the extent of $157,925,000 if the 2 p.m. transfer had been made. There would then have had to be a recall of U.S.$158,500,000 from London on 8 January, with value the previous business day, to restore the peg balance. As no 2 p.m. transfer had been made, the closing balance was in fact U.S.$7,275,000 in credit.

On the morning of 8 January there was an amount of $6,700,000 available to transfer to London. The same amount would have been left as a net credit to the London account if $165.2m. had been transferred at 2 p.m. on 7 January and $158.5m. recalled on 8 January with value the previous day. An instruction for the transfer of U.S.$6,700,000 was prepared. But in the event the computer which kept the accounts in New York was not ordered to effect this transfer, nor was the London branch informed of it.

At 2 p.m. on 8 January the balance to the credit of the New York account was U.S.$161,997,000. After deducting the peg balance of U.S.$500,000 there was a sum of U.S.$161,400,000 available to transfer to London. No transfer was made. Those figures assume, as was the fact, that U.S.$6,700,000 had not been transferred to London in respect of the excess opening balance on that day.

Bankers Trust New York had received payment instructions totalling U.S. $347,147,213.03 for execution on 8 January. All of them had been received by 8.44 a.m. New York time. None of them were executed, for reasons which I shall later explain. (In case it is thought that not even the combined London and New York accounts could have sustained such payments, I should mention that substantial credits were received in New York during 8 January

for the account of the Libyan Bank. If all the payment instructions had been implemented, there would still at the end of the day have been a net balance due to the Libyan Bank on the total of the two accounts)....

Next I turn to the Civil Evidence Act statement of Mr. Brittain, the chairman of Bankers Trust. Late in the afternoon of 7 January he received a telephone call from Mr. Corrigan, the president of the Federal Reserve Bank of New York. Mr. Corrigan asked that Bankers Trust should pay particular attention on the next day to movement of funds on the various Libyan accounts held by Bankers Trust, and report anything unusual to him.

Late in the morning of the next day Mr. Brittain informed the New York Fed. (as it is sometimes called) that "it looked like the Libyans were taking their money out of the various accounts." (So far as the Libyan Bank were concerned, it will be remembered that they had already given instructions for payments totalling over U.S.$347m. on that day.) Later Mr. Brittain learnt that sufficient funds were coming in to cover the payment instructions; he telephoned Mr. Corrigan and told him that the earlier report had been a false alarm. Mr. Corrigan asked Mr. Brittain not to make any payments out of the accounts for the time being, and said that he would revert later.

That assurance was repeated several times during the early afternoon. Mr. Brittain's statement continues:

"Finally I telephoned Mr. Corrigan at about 3.30 p.m. and told him that we now had sufficient funds to cover the payments out of the various Libyan accounts and were going to make them. Mr. Corrigan's response to this was, 'You'd better call Baker' (by which he meant the Secretary of the United States Treasury, Mr. James A. Baker III). I said that I would release the payments and then speak to Mr. Baker. Mr. Corrigan's reply to this was. 'You'd better call Baker first'."

Mr. Brittain was delayed for some 20 minutes talking to Mr. Baker and to an assistant secretary of the Treasury on the telephone. Then at approximately 4.10 to 4.15 p.m. Mr. Baker said: "The President has signed the order, you can't make the transfers."

Mr. Brittain adds in his statement that this was the first occasion on which he became aware that an order freezing the assets was contemplated. In a note made a few weeks after 8 January he adds: "That is how naive I was." I am afraid that I can but agree with Mr. Brittain's description of himself. It seems to me that a reasonable banker on the afternoon of 8 January would have realised, in the light of the first executive order made on the previous day, the requests of Mr. Corrigan, and particularly his saying "You'd better call Baker first," that a ban on payments was a distinct possibility.

There is other evidence as to Mr. Brittain's telephone conversations. First, Mr. Blenk was in Mr. Brittain's office and heard what was said by him. There was not, it seems, any reference by name to Libyan Arab Foreign Bank, but merely to "the Libyans," which meant some six Libyan entities (including the Libyan Bank) which had accounts with Bankers Trust. Secondly, Mr. Sandberg, a senior vice-president of the Federal Reserve Bank of New York, heard Mr. Corrigan's end of the conversations. He accepted in evidence that the New York Fed.

probably knew which Libyan banks held accounts with Bankers Trust.

The Federal Reserve Board Regulations

Considerable emphasis was placed on these Regulations. But in my judgment they are not determinative of anything in this case.

Regulation D imposes a reserve requirement equal to 12 per cent. of the amount of deposits held by banks in the United States. The reserve must be held either in the form of vault cash or as an interest-free deposit with a Federal Reserve Bank. Regulation D accordingly imposes a constraint on the rate of interest which a bank in the United States can offer to depositors. But by section 204 (c)(5) it does not apply "to any deposit that is payable only at an office located outside the United States." That is further defined in section 204.2(t) as a deposit as to which the depositor is entitled "to demand payment only outside the United States." Bankers Trust did not include the Libyan Bank's London account in the deposits for which they maintained a reserve of 12 per cent. in accordance with Regulation D.

There are three possible conclusions which I might draw from that evidence. They are (i) that the sum standing to the credit of the London account was payable only at an office located outside the United States; or (ii) that section 204(c)(5) bears some other meaning than that which it appears to have in plain English; or (iii) that Bankers Trust casually disregarded Regulation D. I have already rejected the first solution, and have found on the evidence of Mr. Van Voorhees and the documents that after December 1980 all operations on the London account were, by express agreement, to be conducted through New York. Consideration of Regulation D and what Bankers Trust did about it does not cause me to have any doubt on that point.

It follows that either section 204(c)(5) does not mean what it appears to say, or else Bankers Trust disregarded it. I do not need to decide which of those alternatives is correct for the purposes of this case. But it does seem in fact that section 204(c)(5) has a somewhat surprising meaning. That appears from the Memorandum of Law of the Federal Reserve Bank of New York ..as amicus curiae in Wells Fargo Asia Ltd. v. Citibank N.A. (1985) 612 F.Supp. 351:

"The location where the depositor has legal right to demand payment is a distinct concept from the location where the deposit is settled. The fact that settlement of United States dollar deposit liabilities takes place in the United States between United States domiciliaries is not determinative of where the deposit is legally payable. Virtually all United States larger-dollar transactions between parties located outside the United States must be settled in the United States. The Clearing House Interbank Payments System or C.H.I.P.S., operated by the New York Clearing House Association for some 140 banks, handles at least U.S.$400 billion in transfers each day, and it is assumed that perhaps 90 per cent. of these payments are in settlement of offshore transactions. If that fact alone were relevant to where a deposit is legally payable, the exemption in Regulation D would almost never apply to foreign-branch deposits

denominated in United States dollars. Clearly, the exemption is not limited to deposits denominated in a foreign currency and is available to foreign branches of United States banks that book deposits denominated in United States dollars."

If there were not some such interpretation the whole Eurodollar market might well be thrown into disarray, or even disappear altogether. In many if not most cases it would be impossible for banks outside the United States to offer the higher interest rates which are a feature of that market.

Whether that doctrine would apply in a case such as the present, where there was an express term that all operations in the London account should be conducted through New York, is something which I need not decide. It would seem to be a generous interpretation which equates that to "payable only at an office located outside the United States." But it does not affect the result in this case.

Nor do I need to mention Regulation Q, F.D.I.C. Insurance or the 3 per cent. reserve requirement for a bank's Euro-currency liabilities.

The demands made

On 28 April 1986 the Libyan Bank sent a telex to Bankers Trust London in these terms: "We hereby instruct you to pay to us at 10.30 a.m. U.K. time on Thursday 1 May 1986 out of our U.S. dollar account number 025-13828 at Bankers Trust London the sum of U.S. dollars one hundred and thirty one million. We make demand accordingly. This sum is to be paid to us in London at the said time and date either by a negotiable banker's draft in such amount (U.S.$131,000,000.00) drawn on Bankers Trust London payable in London to ourselves (Libyan Arab Foreign Bank) or to our order. Alternatively we will accept payment in cash although we would prefer to be provided with a banker's draft as aforesaid."

On the same day a demand in similar terms was made for oe161m., on the basis that this amount should have been transferred from the New York account to the London account at 2 p.m. on 8 January 1986.

Neither demand was complied with. Bankers Trust replied that it would be unlawful (sc. by New York or any other United States law) for them to pay in London. That was factually correct. The question is whether it was relevant. Bankers Trust also denied that the U.S.$161m. transfer should have been made on 8 January.

The action 1986 L. No. 1567 was then started by the Libyan Bank against Bankers Trust. In correspondence between the parties' solicitors various other methods of payment were discussed. In addition the Libyan Bank's solicitors by letter dated 30 July 1986 said that, in so far as notice was required to terminate the managed account arrangement, (1) notice had been given by the Libyan Bank's telex of 28 April 1986 or (2) notice was then given by the solicitors in their letter.

Finally, there was a further demand made in a telex from the Libyan Bank to Bankers Trust on 23 December 1986:

"We now hereby further demand that you pay to us within seven days from receipt of this telex in London, England, the said sums of U.S.$131,000,000 - and U.S.$161,000,000 - respectively, either by the means set out in our April demands or by any other commercially recognised method of transferring funds, which will result in our receiving unconditional payment in London within the said seven-day period.

"In particular (but without prejudice to the foregoing) the said sums of U.S.$131,000,000 - and U.S.$161,000,000 - (or either of them) may be transferred in compliance with these demands by any such commercially recognised method to the U.B.A.F. Bank Ltd. London for the credit of our dollar account number 0000104-416. We reiterate, however that our demands are for us to receive unconditional payment in London within the said seven-day period. If therefore, a transfer or clearing procedure is employed by you to comply with our demands, such procedure must be such that funds or credits said to represent any part of the debt which you owe to us in London are not, in the result, frozen or otherwise impeded in the United States. We would not object to your exercising your right to pay us in sterling, and, if so, our sterling account number at the above bank is 0000103-919."....

(1) The U.S.$131 million claim

(a) Conflict of laws - the connecting factor

There is no dispute as to the general principles involved. Performance of a contract is excused if (i) it has become illegal by the proper law of the contract, or (ii) it necessarily involves doing an act which is unlawful by the law of the place where the act has to be done. I need cite no authority for that proposition (least of all my own decision in Euro-Diam Ltd. v. Bathurst [1987] 2 W.L.R. 1368, 1385) since it is well established and was not challenged. Equally it was not suggested that New York law is relevant because it is the national law of Bankers Trust, or because payment in London would expose Bankers Trust to sanctions under the United States legislation, save that Mr. Sumption for Bankers Trust desires to keep the point open in case this dispute reaches the House of Lords.

There may, however, be a difficulty in ascertaining when performance of the contract "necessarily involves" doing an illegal act in another country. In Toprak Mahsulleri Ofisi v. Finagrain Compagnie Commerciale Agricole et Financiere S.A. [1979] 2 Lloyd's Rep. 98, Turkish buyers of wheat undertook to open a letter of credit "with and confirmed by a first class United States or West European bank." The buyers were unable to obtain exchange control permission from the Turkish Ministry of Finance to open a letter of credit, and maintained that it was impossible for them to open a letter of credit without exporting money from Turkey. It was held that this was no answer to a claim for damages for nonperformance of the contract. Lord Denning M.R. said, at p. 114:

"In this particular case the place of performance was not Turkey. Illegality by the law of Turkey is no answer whatever to this claim. The letter of credit had to be a confirmed letter of credit, confirmed by a first-class West European or U.S. bank. The sellers were not concerned with the

machinery by which the Turkish state enterprise provided that letter of credit at all. The place of performance was not Turkey.
"This case is really governed by the later case of Kleinwort, Sons & Co. v. Ungarische Baumwolle Industrie Aktiengesellschaft [1939] 2 K.B. 678 where bills of exchange were to be given and cover was to be provided in London, but at the same time there was a letter saying, 'We have to get permission from Hungary.' It was said that because of the illegality by Hungarian law in obtaining it, that would be an answer to the case. But Branson J. and the Court of Appeal held that the proper law of the contract was English law; and, since the contract was to be performed in England, it was enforceable in the English courts even though its performance might involve a breach by the defendants of the law of Hungary.
"That case has been quoted in all the authorities as now settling the law. ... The only way that Mr. Johnson (for the Turkish state enterprise) could seek to escape from that principle was by saying - '... Although there was no term, express or implied, in the contract that anything had to be done in Turkey as a term of the contract, nevertheless it was contemplated by both parties. It was contemplated by both parties that the Turkish buyers would have to go through the whole sequence in Turkey of getting exchange control permission, and all other like things: and, if the contemplated method of performance became illegal, that would be an answer. Equally, if it became impossible, that would be a frustration.'
"I am afraid that those arguments do not carry the day. It seems to me in this contract, where the letter of credit had to be a confirmed letter of credit - confirmed by a West European or U.S. bank - the sellers are not in the least concerned as to the method by which the Turkish buyers are to provide that letter of credit. Any troubles or difficulties in Turkey are extraneous to the matter and do not afford any defence to an English contract ..."

From that case I conclude that it is immaterial whether one party has to equip himself for performance by an illegal act in another country. What matters is whether performance itself necessarily involves such an act. The Turkish buyers might have had money anywhere in the world which they could use to open a letter of credit with a United States or West European bank. In fact it would seem that they only had money in Turkey, or at any rate needed to comply with Turkish exchange control regulations if they were to use any money they may have had outsideTurkey. But that was no defence, as money or a permit was only needed to equip themselves for performance, and not for performance itself.

Mr. Sumption took the same route as Mr. Johnson did in the Toprak case. He argued that the court could look at the method of performance which the parties had contemplated, and relied on Regazzoni v. K.C. Sethia (1944) Ltd. [1958] A.C. 301. (Mercifully he refrained from citing Foster v. Driscoll [1929] 1 K.B. 470.) In Regazzoni's case the plaintiff had agreed to buy 500,000 jute bags from the defendants c.i.f. Genoa. It was, of course, open to the defendants as a matter of law to ship the goods to Genoa from anywhere in the world. But in practice the goods had to be obtained from India, both parties knew that this was intended and they also knew that the plaintiff intended to re-export the goods to South Africa. It was illegal by Indian

law, again as both parties knew, to export goods from India destined to South Africa directly or indirectly. The plaintiff's claim failed.

I am relieved from the task of distinguishing between the Toprak principle and Regazzoni's case by a most helpful analysis of Robert Goff J. in the Toprak case itself at first instance which I gratefully adopt. He there held [1979] 2 Lloyd's Rep. 98, 107 that there were two related but distinct principles. The principle of Regazzoni's case was derived from the judgment of Sankey L.J. in Foster v. Driscoll, at pp. 521-522:

"An English contract should and will be held invalid on account of illegality if the real object and intention of the parties necessitates them joining in an endeavour to perform in a foreign and friendly country some act which is illegal by the law of such country notwithstanding that there may be, in a certain event, alternative modes or places of performing which permit the contract to be performed legally."

Even if that principle can be applied to supervening illegality as opposed to illegality ab initio (a point which I would regard as open to question), it does not apply in this case. At no stage was it the real object and intention of the Libyan Bank that any illegal act should be performed in New York. That was not suggested in argument or in the course of the evidence. This case accordingly raises only the other principle, that performance is excused if it necessarily involves doing an act which is unlawful by the law of the place where the act has to be done.

Some difficulty may still be encountered in the application of that principle. For example, if payment in dollar bills in London was required by the contract, it would very probably have been necessary for Bankers Trust to obtain such a large quantity from the Federal Reserve Bank of New York, and ship it to England. That, Mr. Sumption accepts, would not have been an act which performance necessarily involved; it would merely have been an act by Bankers Trust to equip themselves for performance, as in the Toprak case. By contrast, if the contract required Bankers Trust to hand over a banker's draft to the Libyan Bank in London, Mr. Sumption argues that an illegal act in New York would necessarily be involved, since it is very likely that the obligation represented by the draft would ultimately be honoured in New York. I must return to this problem later.

(b) The proper law of the contract

As a general rule the contract between a bank and its customer is governed by the law of the place where the account is kept, in the absence of agreement to the contrary. Again there was no challenge to that as a general rule; the fact that no appellate decision was cited to support it may mean that it is generally accepted....

That rule accords with the principle, to be found in the judgment of Atkin L.J. in N. Joachimson v. Swiss Bank Corporation [1921] 3 K.B. 110, 127, and other authorities, that a bank's promise to repay is to repay at the branch of the bank where the account is kept.

In the age of the computer it may not be strictly accurate to speak of the branch where

the account is kept. Banks no longer have books in which they write entries; they have terminals by which they give instructions; and the computer itself with its magnetic tape, floppy disc or some other device may be physically located elsewhere. Nevertheless it should not be difficult to decide where an account is kept for this purpose, and it is not in the present case. The actual entries on the London account were, as I understand it, made in London, albeit on instructions from New York after December 1980. At all events I have no doubt that the London account was at all material times "kept" in London.

Mr. Sumption was prepared to accept that the proper law governing the London account was English law from 1973 to December 1980. But he submitted that a fundamental change then took place, when the managed account arrangement was made. I agree that this was an important change, and demands reconsideration of the proper law from that date. That the proper law of a contract may be altered appears from Whitworth Street Estates (Manchester) Ltd. v. James Miller & Partners Ltd. [1970] A.C. 583, per Lord Reid at p. 603, and per Lord Wilberforce at p. 615.

Mr. Cresswell for the Libyan Bank submits that there then arose two separate contracts, of which one related to the London account and remained governed by English law; alternatively he says that there was one contract, again governed by English law; or that it had two proper laws, one English law and the other the law of New York. Mr. Sumption submits that there was from December 1980 one contract only, governed by New York law.

Each side has relied on a number of points in support of its contentions. I do not set them out, for they are fairly evenly balanced, and in my view do little or nothing to diminish the importance of the general rule, that the proper law of a bank's contract is the law of the place where the account is kept. Political risk must commonly be an important factor to those who deposit large sums of money with banks; the popularity of Swiss bank accounts with some people is due to the banking laws of the Cantons of Switzerland. And I have already found, on the evidence of Bankers Trust, that the Iranian crisis was at the back of everyone's mind in 1980. Whatever considerations did or did not influence the parties to this case, I believe that banks generally and their customers normally intend the local law to apply. So I would require solid grounds for holding that the general rule does not apply, and there do not appear to me to be such grounds in this case.

I have, then, to choose between the first and third of Mr. Cresswell's arguments - two separate contracts or one contract with two proper laws. It would be unfortunate if the result of this case depended on the seemingly unimportant point whether there was one contract or two. But if it matters, I find the notion of two separate contracts artificial and unattractive. The device of a collateral contract has from time to time been adopted in the law, generally to overcome some formal requirement such as the ci-devant parole evidence rule, or perhaps to avoid the payment of purchase tax, and at times for other purposes. No doubt it has achieved justice, but at some cost to logic and consistency. In my judgment, the true view is that after December 1980 there was one contract, governed in part by the law of England and in part by the law of

New York. It is possible, although unusual, for a contract to have a split proper law, as Mr. Sumption accepted: see Dicey & Morris The Conflict of Laws, 11th ed. (1987), p. 1163 and Chitty on Contracts, 25th ed. (1983), para. 2081. Article 4 of the E.E.C. Convention of 19 June 1980 on the Law Applicable to Contractual Obligations (Official Journal 1980 No. L.266, p. 1) (as I write not yet in force) provides:

"1. To the extent that the law applicable to the contract has not been chosen in accordance with article 3, the contract shall be governed by the law of the country with which it is most closely connected. Nevertheless, a severable part of the contract which has a closer connection with another country may by way of exception be governed by the law of that other country."

That such a solution is not necessarily unacceptable to businessmen is shown by one of the Australian printed forms of charterparty, which adopts it.

Mr. Sumption argues that difficulty and uncertainty would arise if one part of the contract was governed by English law and another by New York law. I do not see that this would be so, or that any difficulty which arose would be insuperable.

There is high authority that branches of banks should be treated as separate from the head office. See for example Reg. v. Grossman (1981) 73 Cr.App.R. 302, where Lord Denning M.R. said, at p. 308:

"The branch of Barclays Bank in Douglas, Isle of Man, should be considered as a different entity separate from the head office in London."

That notion, of course, has its limits. A judgment lawfully obtained in respect of the obligation of a branch would be enforceable in England against the assets of the head office. (That may not always be the case in America.) As with the theory that the premises of a diplomatic mission do not form part of the territory of the receiving state, I would say that it is true for some purposes that a branch office of a bank is treated as a separate entity from the head office.

This reasoning would support Mr. Cresswell's argument that there were two separate contracts, in respect of the London account and the New York account. It also lends some support to the conclusion that if, as in my preferred solution, there was only one contract, it was governed in part by English law and in part by New York law. I hold that the rights and obligations of the parties in respect of the London account were governed by English law.

If I had not reached that conclusion, and if the managed account arrangement was brought to an end as suggested by the Libyan Bank's solicitors in their letter of 30 July 1986, I would have had to consider whether the London account then ceased to be governed by New York law and became governed by English law once more.

(c) The nature of a bank's obligations

It is elementary, or hornbook law to use an American expression, that the customer does not own any money in a bank. He has a personal and not a real right. Students are taught at an early stage of their studies in the law that it is incorrect to speak of "all my money in the

bank." See Foley v. Hill (1848) 2 H.L.Cas. 28, 36, where Lord Cottenham said:
"Money, when paid into a bank, ceases altogether to be the money of the principal ... it is then the money of the banker, who is bound to return an equivalent by paying a similar sum to that deposited with him when he is asked for it ... The money placed in the custody of a banker is, to all intents and purposes, the money of the banker, to do with as he pleases. ..."

Naturally the bank does not retain all the money it receives as cash in its vaults; if it did, there would be no point or profit in being a banker. What the bank does is to have available a sufficient sum in cash to meet all demands that are expected to be made on any particular day.

I mention these simple points in order to clarify the real problem, which is what the obligation of a bank is. There are passages in the experts' reports which appear inconsistent with what I have said. Thus Dr. Marcia Stigum, who gave evidence for Bankers Trust, wrote: "Dollars deposited and dollars lent in wholesale Eurodollar transactions never leave the United States." That statement no doubt makes sense to an economist. For a lawyer it is meaningless.

The obligation of a bank is not, I think, a debt pure and simple, such that the customer can sue for it without warning. Thus in Richardson v. Richardson [1927] P. 228, Hill J. said, at p. 232-233:
"Certain contractual obligations of a bank and its customer, in the absence of special agreement, are well ascertained. They include these implied terms, as stated by Atkin L.J. in Joachimson v. Swiss Bank Corporation [1921] 3 K.B. 110, 127: (a) the promise of the bank to repay is to repay at the branch of the bank where the account is kept, and (b) the bank is not to be called upon to pay until payment is demanded at the branch at which the account is kept. ... If a demand is made at the branch where the account is kept and payment is refused, the position is altered. Undoubtedly the bank is then liable to be sued wherever it can be served."

That in itself is, in my judgment, an answer to one of the ways in which the Libyan Bank put their claim. They cannot sue on a cause of action in debt without more. They must allege a demand made which Bankers Trust were obliged to comply with. Or, to put the point in another way, English law currently recognises that an obligation to pay money can be frustrated: see Ralli Brothers v. Compa ia Naviera Sota y Aznar [1920] 2 K.B. 287, and contrast the view expressed by Dr. F. A. Mann in The Legal Aspect of Money, 4th ed. (1982), pp. 66, 421.

What is the customer entitled to demand? In answering that question one must, I think, distinguish between services which a bank is obliged to provide if asked, and services which many bankers habitually do, but are not bound to, provide. For a private customer with a current account I would include in the first category the delivery of cash in legal tender over the bank's counter and the honouring of cheques drawn by the customer. Other services, such as standing orders, direct debits, banker's drafts, letters of credit, automatic cash tills and foreign currency for travel abroad, may be in the second category of services which the bank is not bound to but usually will supply on demand. I need not decide that point. The answer may depend on the circumstances of a particular case.

The problem in this case does not arise from the current account of a private customer.

There was a correspondent relationship between the two banks, and a call account in London credited with very large sums denominated in United States dollars. The class of demands to which Bankers Trust were obliged to respond may be very different, and must be considered afresh.

It is not, in my judgment, right to assume that the obligation of such a bank is to make payment, and then to look at the charterparty cases in order to discover what "payment" is. In The Brimnes [1975] Q.B. 929, 948, Edmund Davies L.J. said:

"Clause 5 required payment to be made 'in New York in cash in United States currency. ...' The owners' contention, however, that the tendering of the commercial equivalent of cash would suffice found favour with Brandon J. In particular, he concluded that any transfer of funds to M.G.T. for the credit of the owners' account so as to give them the unconditional right to the immediate use of the funds transferred was good payment. In my judgment, that was clearly right. ..."

That was followed in Mardorf Peach & Co. Ltd. v. Attica Sea Carriers Corporation of Liberia [1976] Q.B. 835 (reversed on another point [1977] A.C. 850).

Those cases show, first that the word "cash" in a charterparty does not comprise only pound notes or dollar bills (for the avoidance of doubt, I should say that it has that narrower meaning in this judgment), and secondly that shipping people and banks regard some instruments as the equivalent of cash. Amongst those instruments are a banker's draft and a banker's payment.

(d) Means of transfer

The credit balance of the Libyan Bank with Bankers Trust constituted a personal right, a chose in action. At bottom there are only two means by which the fruits of that right could have been made available to the Libyan Bank. The first is by delivery of cash, whether dollar bills or any other currency, to or to the order of the Libyan Bank. The second is the procuring of an account transfer. (I leave out of account the delivery of chattels, such as gold, silver or works of art, since nobody has suggested that Bankers Trust were obliged to adopt that method. The same applies to other kinds of property, such as land.)

An account transfer means the process by which some other person or institution comes to owe money to the Libyan Bank or their nominee, and the obligation of Bankers Trust is extinguished or reduced pro tanto. "Transfer" may be a somewhat misleading word, since the original obligation is not assigned (notwithstanding dicta in one American case which speak of assignment); a new obligation by a new debtor is created.

Any account transfer must ultimately be achieved by means of two accounts held by different beneficiaries with the same institution. In a simple case the beneficiaries can be the immediate parties to the transfer. If Bankers Trust held an account with the A bank which was in credit to the extent of at least $131m., and the Libyan Bank also held an account at the A bank, it would require only book entries to achieve an account transfer. But still no property is

actually transferred. The obligation of Bankers Trust is extinguished, and the obligation of A bank to Bankers Trust extinguished or reduced; the obligation of A bank to the Libyan Bank is increased by the like amount.

On occasion a method of account transfer which is even simpler may be used. If X Ltd. also hold an account with Bankers Trust London, and the Libyan Bank desire to benefit X Ltd., they instruct Bankers Trust to transfer $131m. to the account of X Ltd. The obligation of Bankers Trust to the Libyan Bank is extinguished once they decide to comply with the instruction, and their obligation to X Ltd. is increased by the like amount. That method of account transfer featured in Momm v. Barclays Bank International Ltd. [1977] Q.B. 790.

In a complex transaction at the other end of the scale there may be more than one tier of intermediaries, ending with a Federal Reserve Bank in the United States. Thus the payer may have an account with B bank in London, which has an account with C bank in New York; the payee has an account with E bank in London, which has an account with D bank in New York. Both C bank and D bank have accounts with the Federal Reserve Bank in New York. When an account transfer is effected the obligations of the New York Fed. to C bank, of C bank to B bank, and of B bank to the payer are reduced; the obligations of the New York Fed. to D bank, of D bank to E bank, and of E bank to the payee are increased. That is, in essence, how the Clearing House Interbank Payments System (C.H.I.P.S.) works, by which a large proportion of transfers of substantial dollar amounts are made.

I shall call the three methods which I have described a correspondent bank transfer, an in-house transfer and a complex account transfer. There are variations which do not precisely fit any of the three, but the principle is the same in all cases. Sooner or later, if cash is not used, there must be an in-house transfer at an institution which holds accounts for two beneficiaries, so that the credit balance of one can be increased and that of the other reduced. In the example of a complex account transfer which I have given that institution is the New York Fed., which holds accounts for C bank and D bank.

Evidence was given by Professor Scott of a method which, at first sight, did not involve an in-house transfer at any institution. That was where different Federal Reserve Banks were used. However, the Professor assured me that an in-house transfer was involved, although it was too complicated to explain. That invitation to abstain from further inquiry was gratefully accepted.

Thus far I have been assuming that only one transaction affecting any of the parties takes place on a given day. But manifestly that is unlikely to be the case; there may be thousands, or tens of thousands. One purpose of a clearing system between banks must be to set off transfers against others, not only between the same parties but also between all other parties to the clearing system. Thus C bank and D bank, in my example of a complex account transfer, may have made many transactions between themselves on the same day. Only the net balance of them all will be credited to one by the New York Fed. and debited to the other at the end. So the identity of the sum which the payer wished to pay to the payee may be entirely

lost in one sense. The net balance may be the other way, and a sum be credited to C bank and debited to D bank instead of vice versa. Or, by a somewhat improbable coincidence, the net balance may be nil.

There are two further complications. The first is that set-off occurs not only between C bank and D bank, but between all other participants to the clearing system. An amount which would otherwise fall to be debited to C bank and credited to D bank may be reduced (i) because F bank has made transfers on that day to C bank, or (ii) because D bank has made transfers on that day to G bank.

Secondly, an intermediate clearing system may be used, such as London dollar clearing. If the chain of transmission on each side reaches a bank that is a member of the London dollar clearing, and if the item in question is eligible for that clearing system, it may be put through it. Then it will go to make up the net credit or debit balances that are due between all the members at the end of the day - and they in turn are settled in New York.

(e) Particular forms of transfer

I set out below those which have been canvassed in this case, and discuss the extent to which they involve activity in the United States.

(i) In-house transfer at Bankers Trust London

This is quite simple, as has been explained. It involves no action in the United States. But it cannot take place unless the Libyan Bank are able to nominate some beneficiary who also has an account with Bankers Trust London.

(ii) Correspondent bank transfer

Again, this is relatively simple and involves no action in the United States. But for it to be effective in this case a bank must be found outside the United States where two conditions are satisfied: the first is that Bankers Trust have a credit balance there of U.S.$131m. or more the second, that an account is also held there for the Libyan Bank or for some beneficiary whom they nominate.

(iii) C.H.I.P.S. or Fedwire

These are two methods of complex account transfer which are used for a high proportion of large dollar transactions. They can only be completed in the United States.

(iv) Banker's draft on London

A banker's draft is, in effect, a promissory note, by which the banker promises to pay to or to the order of the named beneficiary. When the beneficiary receives the draft he can negotiate it, or hand it to another bank for collection. If he negotiates the draft the beneficiary's part in the transaction ends. He has received all that he bargained for, and so far as he is concerned no action in New York is required. Hence the view which emerges in the shipping cases that a banker's draft is as good as cash. But there still remains for the bank the task of honouring the draft when it is presented. The issuing bank, by debiting the customer's account and issuing a draft, has substituted one personal obligation for another. It still has to discharge

the obligation represented by the draft. That it may do, in theory at any rate, by another of the means of transfer that are under discussion - in-house transfer, correspondent bank transfer, C.H.I.P.S., Fedwire, London dollar clearing, cash. So in one sense a banker's draft does not solve the problem; it merely postpones it. One cannot tell whether action is required in the United States until one knows how the draft is to be honoured.

There would be a further problem for the Libyan Bank if they received a draft from Bankers Trust. While the freeze was still operative the draft would in practice be difficult or impossible to negotiate, since nobody would want an instrument made by an American bank which on its face contained a promise to pay to or to the order of the Libyan Bank. That, as it seems to me, would be the case whether the draft was drawn on London or New York. If instead of negotiating the draft the Libyan Bank presented it to another bank for collection, the problem would have been postponed rather than solved for both parties. The Libyan Bank would receive no credit until the draft had been honoured; and Bankers Trust would have to use another means of transfer in order to honour it.

(v) Banker's payment

This is an instrument issued by one bank in favour of another bank. As the shipping cases show, it too is treated as the equivalent of cash in the ordinary way, so that the receiving bank might well allow the customer who presented it to draw against it forthwith. I am not sure whether that would happen in present circumstances, if the receiving bank knew that the banker's payment was issued for the account of the Libyan Bank.

Apart from the possibility of negotiation, which does not arise with a banker's payment, the same problem remains as with a banker's draft. It has to be cleared or honoured (whichever is the right word) by one of the other means of transfer under discussion. Normally the document will specify a clearing system which is to be used.

(vi) London dollar clearing

It may not be right to describe this as a means of transfer in itself, but rather as a method of settling liabilities which arise when other means of transfer are used, such as a banker's draft or banker's payment, or indeed a cheque. Bankers Trust are not themselves members of London dollar clearing, but use it through Lloyds Bank Plc.

Suppose H bank, also a member of the clearing, presented a banker's draft issued by Bankers Trust to or to the order of the Libyan Bank for U.S. $131m. At the end of the day net debits and credits of all the members of the clearing would be calculated - and settled by transfers in New York. As already explained, there would not necessarily be a transfer there of U.S. $131m. or any sum by Lloyds Bank or their New York correspondent to the New York correspondent of H bank. But somewhere in the calculation of the sum that would be transferred by some bank in New York to some other bank in New York the U.S. $131m. would be found.

That is the first aspect of the transaction which requires action in New York. But thus far only the liabilities of the clearing members between themselves have been settled. What of the

liabilities of the banks that have used the clearing but are not members? Bankers Trust owe Lloyds Bank U.S. $131m. That sum will go into a calculation of all the credits and debits between Bankers Trust and Lloyds Bank on that day; the net balance will be settled by a transfer in New York between Bankers Trust New York and Lloyds Bank or their New York correspondent.

Since I have assumed that H bank are a member of the London dollar clearing, no similar transfer is required in their case. They have already received credit for U.S.$131m. in the clearing process and the transfers which settled the balances which emerged from it.

There is another aspect of the London dollar clearing which featured a great deal in the evidence. This is that a rule, at the time unwritten, excluded from the clearing "cheques drawn for principal amounts of interbank Eurocurrency transactions." The system is described in the Child report, where it is said that "by mutual consent 'wholesale' interbank foreign exchange deals and Eurodollar settlements are excluded." That in turn raises a question as to the meaning of "wholesale." Bankers Trust argue that it includes transactions on interest-bearing call accounts between banks, at any rate if they are for large amounts. The Libyan Bank say that it refers only to transactions for time deposits traded between the dealing rooms of banks.

I prefer the evidence of Bankers Trust on this point. The reason for the exclusion appears to be that the introduction of a very large sum by one participant into the clearing system would impose an excessive credit risk. The average value of transactions passing through the system is U.S. $50,000, and the vast majority of items are of the order of U.S. $10,000. It is not normally used for transactions over U.S. $30m.; indeed, there were not many transactions in millions. I find that a transfer of U.S. $131m. by Bankers Trust to or to the order of the Libyan Bank would not, in the circumstances of this case, be eligible for London dollar clearing.

(vii) Other clearing systems outside the United States

Apart from the last point about eligibility, it seems to me that much the same considerations must apply to the other three systems discussed - Euroclear, Cedel and Tokyo dollar clearing. Although the identity of a particular transaction will be difficult or impossible to trace in the net credits or debits which emerge at the end of the clearing, these debits and credits must ultimately be settled in the United States. (The word "ultimately" constantly recurs and is of importance in this case, as was stressed in the course of the evidence.)

But whether that be so or not, there are other points relevant to the use of these systems. Euroclear in Brussels is a system run through Morgan Guaranty Trust Co. for clearing securities transactions and payments in respect of such transactions. If it so happened that Bankers Trust had a credit of U.S. $131m. in the system, it could arrange for that sum to be transferred to the Libyan Bank or any nominee of the Libyan Bank which had an account with Euroclear. That would be a species of correspondent transfer. Alternatively, it could order the transfer to be made anywhere else - but that would involve action in New York.

Cedel, in Luxembourg, is similar to Euroclear in all respects that are material.

The Tokyo dollar clearing system is run by Chase Manhattan Bank at its Tokyo branch. Bankers Trust did not have an account with the system. If they had done, and had used it to pay U.S. $131m. to the Libyan Bank, they would have had to reimburse Chase Manhattan via New York.

(viii) Certificates of deposit

These are issued by banks for large dollar sums, and may be negotiable. Once again they raise the problem that one personal obligation of Bankers Trust would be substituted for another, and the substituted obligation still has to be honoured by some means at maturity. Furthermore, the terms of the certificate would be subject to agreement between the parties, in particular as to its maturity date and interest rate.

(ix) Cash - dollar bills

I am told that the largest notes in circulation are now for U.S. $100, those for U.S. $500 having been withdrawn. Hence there would be formidable counting and security operations involved in paying U.S. $131m. by dollar bills. Bankers Trust would not have anything like that amount in their vault in London. Nor, on balance, do I consider that they would be likely to be able to obtain such an amount in Europe. It could be obtained from a Federal Reserve Bank and sent to London by aeroplane, although several different shipments would be made to reduce the risk. The operation would take some time - up to seven days.

Banks would seek to charge for this service, as insurance and other costs would be involved, and they would suffer a loss of interest from the time when cash was withdrawn from the Federal Reserve Bank to the time when it was handed over the counter and the customer's account debited - assuming that the customer had an interest-bearing account. I cannot myself see any basis on which a bank would be entitled to charge, although there might be a right to suspend payment of interest. If a bank chooses, as all banks do for their own purposes, not to maintain a sum equal to all its liabilities in the form of cash in its vaults, it must bear the expense involved in obtaining cash when a demand is made which it is obliged to meet. If a customer demanded U.S. $1,000 or U.S. $10,000 in cash, I do not see how a charge could be made. When the sum is very much larger it is an important question - which I shall consider later - whether the bank is obliged to meet a demand for cash at all. If it is so obliged, there is not, in my opinion, any right to charge for fulfilling its obligation.

As I have already mentioned, it is accepted that there would be no breach of New York law by Bankers Trust in obtaining such an amount of cash in New York and despatching it to their London office.

(x) Cash - sterling

There would be no difficulty for Bankers Trust in obtaining sterling notes from the Bank of England equivalent in value to U.S. $131m., although, once again, there would be counting and security problems. Bankers Trust would have to reimburse the Bank of England, or the correspondent through whom it obtained the notes, and this would probably be done by a transfer of dollars in New York. But, again, it was not argued that such a transfer would infringe

New York law.

(f) Termination of the managed account arrangement

Those means of transfer are all irrelevant so long as the managed account arrangement subsists; for I have found it to be a term of that arrangement that all the Libyan Bank's transactions should pass through New York. Apart from some minor teething problems at the start in 1980, that term was observed. The only entries on the London call account were credits from, or debits to, the New York demand account. It was the New York account that was used to make payments to, or receive credits from, others with whom the Libyan Bank had business relations. If the arrangement still exists, the London account can only be used to transfer a credit to New York, which would be of no benefit whatever to the Libyan Bank.

In my judgment, the Libyan Bank was entitled unilaterally to determine the managed account arrangement on reasonable notice, which did not need to be more than 24 hours (Saturday, Sundays and non-banking days excepted). The important feature of the arrangement from the point of view of Bankers Trust was that their operators could make payments in New York, on occasion giving rise to an overdraft in New York, safe in the knowledge that there was a credit balance in London which they could call upon and which would not disappear. If it were determined, Bankers Trust New York would be entitled to refuse to make payments which would put the account there into overdraft. For the Libyan Bank an important feature was that they obtained both the speed and efficiency with which current account payments could be made in New York, and the advantage of an account in London bearing interest at Eurodollar rates. If the arrangement were determined and the Libyan Bank began once again to use the London account as if it were a current account, Bankers Trust would be entitled (again on notice) to reduce the rate of interest payable on that account, or to decline to pay interest altogether.

I find nothing surprising in the notion that one party to a banking contract should be able to alter some existing arrangement unilaterally. Some terms, such as those relating to a time deposit, cannot be altered. But the ordinary customer can alter the bank's mandate, for example by revoking the authority of signatories and substituting others, or by cancelling standing orders or direct debits; he can transfer sums between current and deposit account; and he can determine his relationship with the bank entirely. So too the bank can ask the customer to take his affairs elsewhere. In this case it does not seem to me at all plausible that each party was locked into the managed account arrangement for all time unless the other agreed to its determination, or the entire banking relationship were ended. I accept Mr. Cresswell's submission that the arrangement was in the nature of instructions or a mandate which the Libyan Bank could determine by notice. For that matter, I consider that Bankers Trust would also have been entitled to determine it on reasonable notice - which would have been somewhat longer than 24 hours in their case. I hold that the arrangement was determined, implicitly by the Libyan Bank's telex of 28 April 1986, and if that were wrong, then expressly by

their solicitors' letter of 30 July 1986.

What, then, was the position after determination? The New York account remained, as it always had been, a demand account. Subject to New York law, Bankers Trust were obliged to make transfers in accordance with the Libyan Bank's instructions to the extent of the credit balance, but they were not obliged to allow an overdraft - even a daylight overdraft, as it is called when payments in the course of a day exceed the credit balance but the situation is restored by further credits before the day ends. The London account remained an interest-bearing account from which Bankers Trust were obliged to make transfers on the instructions of the Libyan Bank, provided that no infringement of United States law in the United States was involved. If Bankers Trust became dissatisfied with the frequency of such transfers, they were, as I have said, entitled on notice to reduce the rate of interest or bring the account to an end. And if I had not held that the rights and obligations of the parties in respect of the London account were governed by English law at all times, I would have been inclined to hold that they were once more governed by English law when the managed account arrangement was determined, although there is clearly some difficulty in recognising a unilateral right to change the system of law governing part of the relations between the parties.

(g) Implied term and usage

It is said in paragraph 4(2) of the re-re-amended points of defence that there was an implied term that transfer of funds from the London account, whether or not effected through the New York account

"would be effected by instructing a transfer to be made by the defendants' New York Head Office through a United States clearing system to the credit of an account with a bank or a branch of a bank in the United States nominated or procured to be nominated by or on behalf of the plaintiffs for that purpose."

In other words, of the various forms of transfer which I have mentioned, only C.H.I.P.S. or Fedwire were permitted. That term is said to be implied (i) from the usage of the international market in Eurodollars, and (ii) from the course of dealing between the parties since 1980.

Mr. Cresswell submits that such an implied term is implausible on the ground that the foundation of the Eurodollar market is that deposits are not affected by the Federal Reserve requirement which I have mentioned. There may be some force in that. But I prefer to consider the affirmative case for the implication of such a term.

As to usage, I was referred to General Reinsurance Corporation v. Forsakringsaktiebolaget Fennia Patria [1983] Q.B. 856, and particularly the judgment of Slade L.J., at p. 874G:

"There is, however, the world of difference between a course of conduct which is frequently, or even habitually, followed in a particular commercial community as a matter of grace and a course which is habitually followed, because it is considered that the parties concerned have a legally binding right to demand it."

So I must inquire whether it is considered in the international Eurodollar market that creditors have a right to demand payment by C.H.I.P.S. or Fedwire and by no other means.

In Drexel Burnham Lambert International N.V. v. El Nasr [1986] 1 Lloyd's Rep. 356, 365, I cited and followed earlier authority that

"It had been laid down over and over again that the way to prove a custom was to show an established course of business, at first contested but ultimately acquiesced in."

There is no such evidence in this case. Mr. Sumption protests that that is not the only way to prove a usage, though it may be the best way. Of course he is right. So I must consider whether the usage has been proved by other means.

The expert evidence in this case has been immensely helpful in enabling me to understand what happens in the Eurodollar market and how different forms of operation work. But as evidence establishing a usage, or negativing one, it has achieved very little. In that it is similar to many other commercial cases of today. With monotonous regularity parties on the summons for directions apply for leave to call expert evidence of the practice of bankers, or of underwriters, or of insurance brokers, or of others engaged in the market concerned. All too often the evidence shows merely that the expert called by one party believes the contract to mean one thing, and the expert for the other believes that it means something different. But, as I have said, I do not seek to disparage expert evidence which enables the court to understand the market concerned.

The high point of Bankers Trust's case on this issue lies in the expert report of Dr. Stigum from which I quote some brief extracts:

"The usages and practices that apply to wholesale Eurodollar accounts are moreover, well understood by all wholesale participants in the Eurodollar market ... Cash transactions are a feature of only an insignificant portion of total Eurodollar deposits, namely those held by small retail accounts. At the wholesale level, the Eurodollar market is understood by all participants to be a strictly non-cash market. ... All wholesale Eurodollar transactions (these occurring not just in London, but in other centres around the world as well) must, unless they involve a movement of funds from one account at a given bank to another account at that same bank, be cleared in the United States. The reason for this custom and usage is that the ultimate effect of the clearing of a wholesale, Eurodollar transaction is to remove dollars from the reserve account of one bank at the Fed. to the reserve account of another bank at the Fed."

Even as it stands, that passage does not support the implied term pleaded, that transfers would be made "through a United States clearing system." However, it is fair to say that in the particulars of usage there were added by amendment to the points of defence the words "save where book transfers fall to be made between accounts at the same branch" - which would allow, as Dr. Stigum apparently does, both an in-house transfer and a correspondent bank transfer.

Dr. Stigum is an economist and not a banker. I did not find her oral evidence impressive. On the other hand, Mr. Osbourne, who was until 1985 an assistant general manager of

Barclays Bank, did seem to me an impressive witness, whose evidence was very sound on most points. His views were inconsistent with the usage alleged, at any rate in the case of an account such as that of the Libyan Bank with Bankers Trust London.

Furthermore, the supposed usage was inconsistent with the course of dealing between the parties, to which I now turn. It is, of course, true that from December 1980 to January 1986 all transactions by the Libyan Bank were carried out in New York. That is not in itself proof of a course of dealing, since, as I have found, there was an express term to that effect - until the managed account arrangement was brought to an end. What happened between 1973 and December 1980? Fortunately the parties agreed to treat one month as a suitable sample. That was December 1979, in which there were 497 transactions....

The vast majority of those transactions (402) were, as the suggested implied term required, through a United States clearing system. If one adds the in-house transfers of one kind or another in Bankers Trust, as Dr. Stigum's custom permits, the total reaches 488. But there were 9 transactions in that month alone (London bank drafts and a London banker's payment) which were not permitted, either by the implied terms which Bankers Trust allege or by Dr. Stigum's custom and usage, although they may very well have been for relatively small amounts.

I find difficulty in seeing how course of dealing by itself could support a negative implied term of the kind alleged. The phrase is often used to elucidate a contract or to add a term to it. But if course of dealing is to eliminate some right which the contract would otherwise confer, I would require evidence to show, not merely that the right had never been exercised, but also that the parties recognised that as between themselves no such right existed. In other words, there must be evidence establishing as between the parties what would be a usage if it applied to the market as a whole. But whether that be so or not, I find no implied term such as Bankers Trust allege to be established either by usage, or by course of dealing, or by both.

There was a great deal of evidence as to which Eurodollar transactions could be described as "wholesale" and which as "retail." I am inclined to think that the answer depends on the purpose for which the description is used. I have found that a payment of U.S. $131m. by Bankers Trust to the Libyan Bank would be excluded from London dollar clearing. In that context it may, perhaps, be described as wholesale. But I have also found that no usage applies to the Libyan Bank's account. I do not exclude the possibility that some usage applies to time deposits traded between the dealing rooms of banks. If the word "wholesale" is applied to that class of business, the Libyan Bank's account is not within it.

(h) Obligations in respect of the London account

Having considered and rejected the two methods by which Bankers Trust seek to limit their obligations in respect of the London account - that is, an express term from the managed account arrangement still subsisting, or an implied term - I have to determine what those obligations were. What sort of demands were the Libyan Bank entitled to make and Bankers

Trust bound to comply with? As I said, earlier, it is necessary to distinguish between services which a bank is obliged to provide if asked, and services which many bankers do provide but are not obliged to.

Dr. F. A. Mann in his book The Legal Aspect of Money, 4th ed. (1982), pp. 193-194, discusses this question in the context of the Eurodollar market. I have given careful attention to the whole passage. His conclusion is:

"The banks, institutions or multinational companies which hold such deposits, frequently of enormous size, and which deal in them are said to buy and sell money such as dollars. In law it is likely, however, that they deal in credits, so that a bank which has a large amount of dollars standing to the credit of its account with another (European) bank probably does not and cannot expect it to be 'paid' or discharged otherwise than through the medium of a credit to an account with another bank. In the case of dollars it seems to be the rule (and therefore possibly a term of the contract) that such credit should be effected through the Clearing House Interbank Payments System (C.H.I.P.S.) in New York. ... In short, as economists have said, the Eurodollar market is a mere account market rather than a money market."

Dr. Mann cites Marcia Stigum's book, The Money Market (1978) and finds some support for his view - which he describes as tentative - in an English case which has not been relied on before me. The passage in question appeared for the first time in the 1982 edition of Dr. Mann's book after the litigation about the Iranian bank freeze.

I am reluctant to disagree with such a great authority on money in English law, but feel bound to do so. There is one passage, at p. 194, which appears to me to be an indication of economic rather than legal reasoning:

"it could often be a national disaster if the creditor bank were entitled to payment, for in the last resort this might mean the sale of a vast amount of dollars and the purchase of an equally large sum of sterling so as to upset the exchange rates."

But if a person owes a large sum of money, it does not seem to me to be a sound defence in law for him to say that it will be a national disaster if he has to pay. Countries which feel that their exchange rates are at risk can resort to exchange control if they wish.

Furthermore, the term suggested by Dr. Mann - that all payments should be made through C.H.I.P.S. - is negatived by the evidence in this case. It may for all I know be the rule for time deposits traded between the dealing rooms of banks, but I am not concerned with such a case here.

R. M. Goode, in Payment Obligations in Commercial and Financial Transactions (1983), p. 120, writes:

"Would an English court have declared the Executive Order effective to prevent the Iranian Government from claiming repayment in London of a dollar deposit maintained with a London bank? At first blush no, as it is unlikely that an English court would accord extra-territorial effect to the United States Executive Order. However, the argument on the United States side (which

initially appeared to have claimed extra-territorial effect for the Order) was that in the Eurocurrency market it is well understood that deposits cannot be withdrawn in cash but are settled by an inter-bank transfer through the clearing system and Central Bank of the country whose currency is involved. So in the case of Eurodollar deposits payment was due in, or at any rate through, New York, and the Executive Order thereby validly prevented payment abroad of blocked Iranian deposits, not because the order was extraterritorial in operation but because it prohibited the taking of steps within the United States (i.e. through C.H.I.P.S. in New York) to implement instructions for the transfer of a dollar deposit located outside the United States."

That was published in 1983. I have not accepted the argument which Professor Goode refers to, that it is well understood that deposits cannot be withdrawn in cash. I find that there was no implied term to that effect.

I now turn again to the forms of transfer discussed in subsection (e) of this judgment, in order to consider in relation to each whether it was a form of transfer which the Libyan Bank were entitled to demand, whether it has in fact been demanded, and whether it would necessarily involve any action in New York.

(i) In-house transfer at Bankers Trust London

(ii) Correspondent bank transfer

I consider that each of these was a form of transfer which the Libyan Bank were entitled to demand as of right. But I find that no demand has in terms been made for a transfer by either method. This may well be because, in the case of an in-house transfer, there is no other institution with an account at Bankers Trust London which the Libyan Bank wish to benefit; and in the case of a correspondent bank transfer, the Libyan Bank have been unable to nominate a bank outside the United States which holds accounts both for Bankers Trust and also for the Libyan Bank or some beneficiary whom they wish to nominate. It is not shown that U.B.A.F. Bank Ltd. (referred to in the telex of 23 December 1986) fulfilled this requirement.

As to action in New York, none would have been required in respect of an in-house transfer at Bankers Trust London. Whether any would have been required in the case of a correspondent bank transfer depends on whether the correspondent bank in question did or did not already owe Bankers Trust U.S. $131m. or more. On the evidence, it is at the least unlikely that any bank outside New York could be found owing Bankers Trust U.S. $131m.

(iii) C.H.I.P.S. or Fedwire

There is no doubt that the Libyan Bank were entitled to demand such a transfer. But they did not demand it. Such a transfer would have required action in the United States which was illegal there. The only doubt which I have felt on that point is as to whether the ultimate entries on the books of a Federal Reserve bank would have been so remote from the underlying transaction - being perhaps between different parties, for a different sum, and even in the opposite direction to the underlying transaction - that they would not be unlawful.

Professor Felsenfeld, who gave evidence on behalf of the Libyan Bank, was inclined to think that such a transaction would be unlawful, and so was Mr. Knake. Professor Scott took a different view. Whichever be correct, I am convinced that some illegal action in the United States would be required by a C.H.I.P.S. or Fedwire transfer.

(iv) Banker's draft on London
(v) Banker's payment

Bankers Trust did not in practice issue banker's drafts on their London office. Instead they would provide a cheque drawn on Lloyds Bank Plc. That does not seem to me a point of much importance. I consider that Bankers Trust were obliged to provide such instruments to the Libyan Bank if asked to do so, subject to one important proviso - that the instruments were eligible for London dollar clearing. If they were not, then there was no such obligation, since in normal times and in the absence of legislation it would be simpler to use C.H.I.P.S. or Fedwire in the first place.

A banker's draft was demanded in the telex of 28 April 1986; and a banker's payment was within the description "any other commercially recognised method of transferring funds" demanded by the telex of 23 December 1986. But since, as I have found, an instrument for U.S. $131m. would not have been eligible for London dollar clearing in the circumstances of this case, Bankers Trust were not obliged to comply with that aspect of the demands.

It was argued that Bankers Trust might still have made interest payments through the London dollar clearing, since the exclusion is only of the principal amount of inter-bank Eurocurrency transactions. There are, in my judgment, three answers to that point. First, it is not relied on in the points of claim; secondly, there was no demand for interest payments as such; thirdly, the interest due had been capitalised once credited to the account. Indeed, if that were not so it would be impossible, or very difficult, to say how much of the U.S. $131m. was interest.

That makes it unnecessary to answer the question, which I regard as particularly difficult, whether the issue of a banker's draft or banker's payment by Bankers Trust to the Libyan Bank would necessarily involve illegal action in New York. Even if the instrument were cleared through London dollar clearing, action in New York would, as I have already mentioned, ultimately be required. (The same is true, in all likelihood, if one of the other clearing systems outside the United States had been used.) Although the identification of a particular payment would be even more difficult than in the case of a straight C.H.I.P.S. transfer, I am inclined to believe that Bankers Trust would have a second defence to a claim based on failure to issue such an instrument, on the ground that performance of their obligation would necessarily involve illegal action in New York. However, Mr. Sumption appeared at one stage to accept that the issue of a draft drawn on London would not, or might not, involve illegal action in New York.

I need not consider problems as to the worth of a banker's draft or banker's payment to the Libyan Bank in present circumstances or the damages they would have suffered by not

obtaining one.

(vi) London dollar clearing

(vii) Other clearing systems outside the United States

In effect these have already been considered. Bankers Trust were not obliged to issue an instrument with a view to its being passed through London dollar clearing if it was not eligible; and an instrument for U.S. $131m. in this case would have been disqualified.

The other clearing systems give rise to similar problems. There is no evidence that Bankers Trust had an existing credit of U.S. $131m. with Euroclear or Cedel arising from a transaction in securities, and they were under no obligation to acquire one. Nor were they obliged to become participants in the Tokyo dollar clearing. If they had done so, the issue of an instrument to be cleared in Tokyo would, as with London dollar clearing, have necessarily involved action that was illegal in the United States.

(viii) Certificates of deposit

The issue of these comes in my judgment into the class of service which banks habitually do provide but are not obliged to. If for no other reason, that is because agreement is involved, as to the maturity of the instrument and the interest rate. It cannot be that a customer is entitled to demand any maturity and any interest rate that he chooses. Nor would a reasonable maturity and a reasonable interest rate provide a practical solution.

In addition there would again be the problem whether a certificate of deposit could be honoured at maturity without infringing the law of the United States; and whether the Libyan Bank had suffered any damage by not obtaining one.

(ix) Cash - dollar bills

Of course it is highly unlikely that anyone would want to receive a sum as large as U.S. $131m. in dollar bills, at all events unless they were engaged in laundering the proceeds of crime. Mr. Osbourne said in his report:

"As to the demand for payment in cash, I regard this simply as the assertion of a customer's inalienable right. In practice, of course, where such a large sum is demanded in this manner, fulfilment of the theoretical right is unlikely, in my experience, to be achieved. sensible banker will seek to persuade his customer to accept payment in some more convenient form, and I have yet to encounter an incident of this nature where an acceptable compromise was not reached, even where the sum was demanded in sterling."

I would substitute "fundamental" for "inalienable"; but in all other respects that passage accords with what, in my judgment, is the law. One can compare operations in futures in the commodity markets: everybody knows that contracts will be settled by the payment of differences, and not by the delivery of copper, wheat or sugar as the case may be; but an obligation to deliver and accept the appropriate commodity, in the absence of settlement by

some other means, remains the legal basis of these transactions. So in my view every obligation in monetary terms is to be fulfilled, either by the delivery of cash, or by some other operation which the creditor demands and which the debtor is either obliged to, or is content to, perform. There may be a term agreed that the customer is not entitled to demand cash; but I have rejected the argument that there was any subsisting express term, or any implied term, to that effect. Mr. Sumption argued that an obligation to pay on demand leaves very little time for performance, and that U.S. $131m. could not be expected to be obtainable in that interval. The answer is that either a somewhat longer period must be allowed to obtain so large a sum, or that Bankers Trust would be in breach because, like any other banker they choose, for their own purposes, not to have it readily available in London.

Demand was in fact made for cash in this case, and it was not complied with. It has not been argued that the delivery of such a sum in cash in London would involve any illegal action in New York. Accordingly I would hold Bankers Trust liable on that ground.

(x) Cash - sterling

Dicey & Morris, The Conflict of Laws, 11th ed. state in Rule 210, at p. 1453:

"If a sum of money expressed in a foreign currency is payable in England, it may be paid either in units of the money of account or in sterling at the rate of exchange at which units of the foreign legal tender can, on the day when the money is paid, be bought in London ..."

See also Chitty on Contracts, 25th ed., para. 2105:

"Where a debtor owes a creditor a debt expressed in foreign currency ... the general rule is that the debtor may choose whether to pay in the foreign currency in question or in sterling."

Mr. Sumption argues that there is no such rule, at any rate since the decision in Miliangos v. George Frank (Textiles) Ltd. [1976] A.C. 443, that the judgment of an English court does not have to be given in sterling.

Since the Miliangos decision the rule in Dicey & Morris, or rather an earlier version of it, has been approved obiter by Mocatta J. in Barclays Bank International Ltd. v. Levin Brothers (Bradford) Ltd. [1977] Q.B. 270, 278. It must be admitted that the foundations of the rule appear to be somewhat shaky, and the reasoning upon which it has been supported open to criticism. Furthermore, in George Veflings Rederi A/S v. President of India [1979] 1 W.L.R. 59, Lord Denning M.R. said, at p. 63:

"I see no reason to think that demurrage was payable in sterling. So far as demurrage was concerned, the money of account was U.S. dollars and the money of payment was also U.S. dollars ... When you find, as here, that the demurrage is to be calculated in U.S. dollars and that there is no provision for it to be paid in sterling, then it is a reasonable inference that the money is payable in U.S. dollars."

The rule in Dicey & Morris had been cited in the court below in that case; and it would appear at first sight that the Master of the Rolls disagreed with it. However, his conclusion evidently was that by implication the contract provided that demurrage should be paid only in

U.S. dollars. In other words, the parties had contracted out of the rule. Furthermore, in that case a payment in sterling had in fact been made. The issue was not whether the charterer was entitled to pay in sterling, but how much credit should be given for the payment which he had made.

The pendulum swung the other way in In re Lines Brothers Ltd.[1983] Ch. 1. Both the Barclays Bank case and the George Veflings case were cited in argument. Oliver L.J., speaking of the argument of counsel for the creditors, said, at p. 25:

"Now his argument has an engaging - indeed an almost unanswerable - logic about it once one accepts his major premise, but it is here that I find myself unable to follow him, for what, as it seems to me, he is seeking to do is to attribute to the Miliangoscase a greater force than it has in fact. In effect what he seeks to do is to suggest that because Miliangos establishes that a creditor in foreign currency is owed foreign currency, it follows that the debtor is a debtor in foreign currency alone and cannot obtain his discharge by anything but a foreign currency payment. But this is to stand Miliangos on its head. What Miliangos is concerned with is not how the debtor is to be compelled to pay in the currency of the debt but the measure of his liability in sterling when, ex hypothesi, he has not paid and is unwilling to pay in the currency of the debt."

That, as it seems to me, is authority of the Court of Appeal that the Miliangos case does not affect the question whether a foreign currency debtor has a choice between payment in sterling and payment in foreign currency. I should follow the dicta of Oliver L.J. and Mocatta J., and the passages cited from Dicey & Morris, The Conflict of Laws, 11th ed. and Chitty on Contracts, 25th ed. That is also Dr. Mann's preferred solution and has the support of the Law Commission.

Still it may be agreed, expressly or by implication, that the debtor shall not be entitled to pay in sterling. There is no subsisting express term to that effect in the present case. Nor do I consider that such a term should be implied, in the present context of a banking contract where the obligation of Bankers Trust is to respond to demands of the Libyan Bank.

It remains to be considered whether there is a true or business option (see Chitty, para. 1387), such that payment in dollars is the primary or basic obligation but the debtor may choose to pay in sterling if it suits him to do so. Or are there alternative methods of performance, with the consequence described by Lord Devlin in Reardon Smith Line Ltd. v. Ministry of Agriculture, Fisheries and Food [1963] A.C. 691, 730:

"Where there is no option in the business sense, the consequence of damming one channel is simply that the flow of duty is diverted into the others and the freedom of choice thus restricted."

No other authority was cited on the point, and I feel that the material on which to decide it is somewhat meagre. Given that a foreign currency debtor is entitled to choose between discharging his obligations in foreign currency or sterling, I consider that he should not be entitled to choose the route which is blocked and then claim that his obligation is discharged or suspended. I prefer the view that he must perform in one way or the other; so long as both

routes are available he may choose; but if one is blocked, his obligation is to perform in the other.

A further complication arises from the fact that a bank's obligation is to respond to a demand, and there are or may be various different kinds of demand which a customer is entitled to make. When the general doctrine of Dicey & Morris, The Conflict of Laws, is considered in the context of a bank account such as that of the Libyan Bank, and there is (as I have held) no express or implied term that the obligation must be discharged only in dollars, I hold that the customer is entitled to demand payment in sterling if payment cannot be made in dollars. (I need not decide whether payment in sterling could be demanded if it was still possible to pay in dollars.) In this case there was an alternative demand for sterling in the telex of 23 December 1986; and it is not suggested that this would have involved any illegal activity in New York. I am not sure that it was a demand specifically for sterling notes, rather than an account transfer in sterling. But if the Libyan Bank were entitled to demand sterling, no separate point arises as to the manner in which it should be provided. So if I had not held that payment should have been made in cash in United States dollars, I would have held that it should have been made in sterling.

(2) The claim that a further sum should have been transferred from New York

This arises in three different ways on the facts. First it is said that U.S. $165.2m. should have been transferred to London at 2 p.m. on 7 January 1986.

Bankers Trust have two answers to this claim. First they say that instructions had been received and were pending for further payments to be made on 7 January after 2 p.m., which exceeded the amount then standing to the credit of the New York account (and, for that matter, the London account as well). It was only because further receipts also occurred after 2 p.m. that the New York account ended the day with a credit balance of U.S. $7.275m., and the London account remained untouched.

Secondly, Bankers Trust say that, if they were obliged to make a transfer to London on 7 January, they could lawfully have postponed it until after 8.06 p.m. New York time, when the first Presidential order came into force. Thereafter, they say, the transfer would have been illegal because it would have left the New York account overdrawn and would have constituted the grant of credit or a loan to the Libyan Bank.

In my judgment both those arguments fail. The telex of 27 November 1986, from which I have already quoted, contained this passage:

Each day, at 2 p.m., the balance position of your account is determined and any credits received up to that time, less payments and less the peg balance, are immediately invested."

It is said that "payments" there are not confined to payments actually made, and include payments for which instructions were pending. In view of the precision with which the time of 2

p.m. is stated, and the word "immediately," I do not consider that to be right. Mr. Sumption argued that "immediately" is coloured (one might say contradicted) by the illustration given in the telex; but I do not agree. The argument that Bankers Trust were entitled to delay the transfer until after 8.06 p.m. also fails, for the same reason, and it is unnecessary to decide whether it would have been a breach of the first Presidential order to allow an overdraft in New York which was less than the credit balance in London. They would certainly have been entitled in any event not to make payments which exceeded the net credit balance of the two accounts. But after credits which were received during the afternoon there was no need to do that.

Mr. Sumption also argued that the passage in the telex set out above was merely an illustration of how the arrangement would work, and not part of the revised terms of the managed account arrangement. That argument I also reject.

Some attention was paid to the course of dealing on these points. Mr. Blackburn's evidence showed that there was no consistency in the treatment of unprocessed payments; sometimes they were taken into account in deciding whether a 2 p.m. transfer should be made, and at other times they were ignored. As to the actual timing of the transfer, it was always booked in New York on the same day, and in London on the following day with one day's back value. The important feature to my mind is that, so long as there was no legislative interference, it did not make any difference to the parties whether the actual transfer was made at 2 p.m. or at any time up to midnight. Banking hours in London had already ended. Nor did it necessarily make a difference whether unprocessed payments were taken into account; if they were not, and a debit balance in New York resulted at the end of the day, Bankers Trust would recall an appropriate amount next morning from London, with one day's back value. It was only when the Presidential orders came to be made that timing became important. Bankers Trust were, as I hold, in breach of contract in failing to transfer U.S. $165.2m. to London at 2 p.m. on 7 January.

If they had done so, they would have been entitled to recall U.S. $158.5m. from London next morning, so that the net loss to the London account was only U.S. $6.7m. Mr. Cresswell argues that, in practice, Bankers Trust only recalled sums from the London account late in the day, and therefore after 4.10 p.m. when the second Presidential order came into effect; a transfer from London would thereafter have been illegal. In point of fact that may well be correct. But I have no doubt at all that, if there had been a large overdraft on the New York account on the morning of 8 January 1986, Bankers Trust would on that particular day have recalled the appropriate sum from London with the utmost despatch.

No transfer to London having in fact been made on 7 January, and no recall the next morning, U.S. $6.7m. should then have been transferred, as the amount by which the New York balance exceeded the peg of U.S.$500,000. The only issue of potential importance here is whether the transfer was actually made. Although preparations were made for effecting the transfer, I am satisfied that it was countermanded and did not take effect. There is no need for me to decide precisely when the transfer ought to have been made, since that is subsumed in the next point.

The Libyan Bank's third complaint under this head is that, no transfers between New York and London having in fact been made at 2 p.m. on 7 January or in the morning of 8 January, the balance in New York at 2 p.m. on 8 January was U.S. $161,997,000. It is said that a sum of U.S. $161.4m. should then have been transferred to London. In answer to that Bankers Trust rely on points that are the same as, or similar to, those raised in respect of 2 p.m. on 7 January: they say that they were entitled to take pending payment instructions into account; and that they were entitled to delay payment until after 4.10 p.m. when the second Presidential order had been made, which certainly prohibited such a transfer. I reject both arguments for the reasons already given, based on the telex of 27 November 1985. It is true that if the pending payment instructions were to be executed in the afternoon, there were grounds for apprehension that the New York account would become overdrawn, which might be a breach of the first Presidential order; and even that the total of both accounts would be overdrawn, which would plainly be a breach of that order. The solution for Bankers Trust was not to execute those pending instructions unless and until further credits were received in New York. Some were in fact received - the New York account ended the day in credit to the extent of U.S. $251,129,000. Payment instructions for that day totalled U.S. $347,147,213.03, and none of them were in fact executed. So on any view the New York account would have been overdrawn if all had been executed, and that much more overdrawn if in addition U.S. $161.4m. had been transferred to London at 2 p.m. But the net total of the two accounts would still have been a credit balance. If Bankers Trust took the view that an overdraft on the New York account would itself be a breach of the Presidential order, and if they were right, the solution as I have said was to execute the pending instructions only as and when credits received permitted them to do so.

Accordingly I hold that (i) Bankers Trust were in breach of contract in failing to transfer U.S. $165.2m. to London at 2 p.m. on 7 January; (ii) if they had done that, they could and would have recalled U.S. $158.5m. from London in the morning of 8 January; but, (iii) on the assumption that both those steps had been taken, there would have been a further breach in failing to transfer U.S. $154.7m. to London at 2 p.m. on 8 January. (I trust that the calculation of this last figure is not too obscure. The 2 p.m. transfer on 8 January should have been U.S. $161.4m. if neither of the previous transfers had been made - as in fact they were not. If they had both been made, the figure would have been reduced to U.S. $154.7m.)

The balance resulting from those three figures is a net loss to the London account of U.S. $161.4m. I hold that this must be added to the Libyan Bank's first claim, as an additional sum for which that claim would have succeeded but for breaches of contract by Bankers Trust. It is said that this loss is not recoverable, because it arose from a new intervening act and is too remote. In the circumstances as they were on 7 and 8 January I have no hesitation in rejecting that argument.

(3) Failure to comply with payment instructions

As pleaded, the Libyan Bank's case is that their payment instructions on 8 January 1986 ought to have been honoured to the extent of U.S. $226,147,213.88, and were not. That figure is calculated in Mr. Blackburn's exhibit C.8. It assumes (i) a transfer of U.S. $6.7m. to London on the morning of 8 January, (ii) no 2 p.m. transfer on 7 or 8 January, and (iii) that the New York account is not allowed to become overdrawn at any time. So for this purpose the Libyan Bank are content to accept that an overdraft on the New York account alone would be a breach of the first Presidential order. Or else they are assuming the success of their claim (1) for U.S. $131m., in which case the maximum for which claim (3) can succeed is the figure stated above.

I have to approach it on a different assumption, in the light of my conclusions hitherto. If a net total of U.S. $161.4m. had been transferred to London by 2 p.m. on 8 January, the payments that could have been made before 4.10 p.m. would have totalled some U.S. $89m. I am satisfied that in the ordinary way those payments would have been made before 4.10 p.m. The last credit that day was received at 3.03 p.m., which would have left sufficient time for the processing of payment instructions, and C.H.I.P.S. normally closed at 4.30 p.m., although on this occasion it was extended first to 5 p.m. and then to 5.30 p.m. I am also satisfied that the reason no payments were made was apprehension that this might be unwelcome to the Federal Reserve Bank of New York or the Treasury if a freeze were imminent. Nevertheless I do not consider that there was any breach of contract by Bankers Trust in not making any payments before 4.10 p.m., when it became illegal for them to carry out their instructions. There obligation was to make the payments that day, and not at any particular time in the day. Mr. Cresswell submitted that there was an implied term that Bankers Trust would not act on the instructions of a third party. I do not see why that should be so. Provided that they were not in breach of any obligation as to acting on the instructions of their customer, it does not seem to me to matter whether they acted on their own initiative or at the suggestion of somebody else.

In any case, if failure to make the payments had been a breach of contract it would have caused the Libyan Bank no loss. One might suppose that all or at any rate most of the payments were designed to discharge liabilities of the Libyan Bank or to create new obligations owed to the Libyan Bank, although it is always a possibility that some of them may have been ordered for no consideration in favour of causes which the Libyan Bank desired to support. But the Libyan Bank have expressly declined to put forward a case that they have had to or will have to make the payments from other sources, or that they have not obtained credits from others which otherwise they would have obtained. They prefer to take their stand on the point that they now have a credit balance which is frozen in New York, which they would not have had if the payments had been made. As a matter of law that does not seem to me a sufficient allegation of loss. Nor do I think that any case of injury to the Libyan Bank's reputation has been made out.

Claim (3) therefore fails, on two grounds.

(4) Breach of duty of confidence

The facts as I have found them are that in the morning of 8 January 1986 Mr. Brittain of Bankers Trust told the Federal Reserve Bank of New York that "it looked like the Libyans were taking their funds out of the various accounts." Later he told Mr. Corrigan that this earlier report had been a false alarm - meaning, I suppose, that funds were coming in to replace payments that had been ordered. There was no mention of Libyan Arab Foreign Bank by name. But the New York Fed. probably knew which Libyan banks held accounts with Bankers Trust.

Neither side suggests that New York law as to the duty of confidence owed by a banker to his customer is any different from English law. Nor is it argued that the information was given under compulsion of law. But Bankers Trust say that they were entitled to act as they did (a) because their own interests required them to do so, (b) because the Libyan Bank must be taken impliedly to have consented, or (c) pursuant to a higher public duty. In that connection I was referred to Tournier v. National Provincial and Union Bank of England [1924] 1 K.B. 461. There Bankes L.J. included, at p. 473: "where there is a duty to the public to disclose" among the exceptions to a banker's duty of confidence.

Scrutton and Atkin L.JJ. on the other hand spoke of the duty to prevent fraud or crime, at pp. 481 and 486.

I do not accept that disclosure was required in Bankers Trust's own interests, in the sense of the first exception relied upon; or that there was implied consent by the Libyan Bank. But I have more difficulty over the point about higher public duty. In England there is statutory power in section 4(3) of the Bank of England Act 1946 and section 16 of the Banking Act 1979 for the Bank of England to obtain information from banks. It was not argued that I should presume a similar legal power in the New York Fed. in relation to banks in New York. But presuming (as I must) that New York law on this point is the same as English law, it seems to me that the Federal Reserve Board, as the central banking system in the United States, may have a public duty to perform in obtaining information from banks. I accept the argument that higher public duty is one of the exceptions to a banker's duty of confidence, and I am prepared to reach a tentative conclusion that the exception applied in this case.

I need not reach a final conclusion on that point, because I am convinced that any breach of confidence there may have been caused the Libyan Bank no loss. It is not suggested, and there is no evidence to show, that the second Presidential order would not have been made when it was but for the information passed by Mr. Brittain to the New York Fed. What is suggested is that, if that information had not been passed, the payments would have been made before 4.10 p.m. I am not convinced as to that. Suppose that Mr. Brittain had talked to the New York Fed. in a way that involved no breach of confidence - for example by asking whether he could lawfully make a large payment in the light of the first Presidential order; the result would in all probability have been exactly the same. Any breach of confidence was incidental. It did not of itself cause the payments not to be made. And even if it did, I have held in section (3) above that the Libyan Bank have not established any loss by reason of the fact that the payments were not made.

Claim (4) also fails.

(5) Frustration

This claim is pleaded as an alternative ground for awarding the Libyan Bank the relief sought under claims (1) and (2). Since I have held that those two claims succeed, I can deal briefly with the topic of frustration.

Section 1 of the Law Reform (Frustrated Contracts) Act 1943 provides:
"(1) Where a contract governed by English law has become impossible of performance or been otherwise frustrated, and the parties thereto have for that reason been discharged from the further performance of the contract ... (2) All sums paid or payable to any party in pursuance of the contract before the time when the parties were so discharged ... shall, in the case of sums so paid, be recoverable from him ..."

It is said that the U.S. $131m. credit in the London account, and the additional amount of U.S. $161.4m. which should have been transferred to the London account, are the balance of sums paid in the past by the Libyan Bank to Bankers Trust; that the contract between them has become impossible of performance or been frustrated, by reason of the Presidential order prohibiting repayment; and that consequently those sums are recoverable from Bankers Trust under section 1 of the Act or at common law.

So paradoxical an argument requires scrutiny. The first answer to it is in my judgment that the obligation of Bankers Trust was suspended but not discharged: Arab Bank Ltd. v. Barclays Bank (Dominion Colonial & Overseas) Ltd. [1954] A.C. 495, and see also the observations made in the Court of Appeal in that case [1953] 2 Q.B. 527. Mr. Cresswell seeks to distinguish that case on the ground that special rules apply to the outbreak of war. That is no doubt true to some extent; but I see no ground for holding that war has a different effect on the obligations of a banker from any other kind of supervening illegality for present purposes. Accordingly I would hold that the contract as a whole has not become impossible of performance or been otherwise frustrated; or at any rate that the parties have not been altogether discharged from further performance.

A second answer is, I think, that payments made by the Libyan Bank to Bankers Trust were not paid "in pursuance of the contract." There was no obligation on the Libyan Bank to deposit sums with Bankers Trust. So these were not payments comprised within section 1 of the Act.

As to the alternative restitutionary remedy at common law, the consideration given by Bankers Trust has not wholly failed. They are still obliged to repay one day, and meanwhile to credit interest to the account.

If it had been material, I would have held that claim (5) failed.

(6) Failure to make transfers in due time between April 1984 and November 1985

Logically this claim might have been considered first, since it is not at all concerned with

the freeze but with events that occurred earlier.

The facts are that from December 1980 onwards under the managed account arrangement Bankers Trust were obliged to review the New York account every morning, and transfer the excess of U.S. $500,000 in multiples of U.S. $100,000 to the interest-bearing call account in London with value the previous day. What they in fact did from April 1984 onwards was to review the account at 2 p.m., and make a transfer to London if appropriate on the basis of that review with value that day. Bankers Trust did not lose by the change, since a further transfer from London with that day's value was made if operations between 2 p.m. and the close of business diminished the New York account below U.S. $500,000. If, on the other hand, those operations increased the closing balance above U.S. $599,999, the Libyan Bank did lose, because they did not obtain that day's value in their London interest-bearing account for the excess, but only the next business day's value. They would lose interest for one day, or for three days if a week-end intervened.

The change was made unilaterally by Bankers Trust, after they had unsuccessfully tried to persuade the Libyan Bank to agree to an increase in the peg balance, and without informing the Libyan Bank. Later, in November 1985, it is accepted that the Libyan Bank did agree to it prospectively. It has not been suggested that the change was anything other than a breach of contract at the time when it first occurred in April 1984; nor that there would be any defence to the claim in English law. But it is said that, under New York law, the Libyan Bank are precluded from relying upon the breach by their failure to complain about entries in their bank statements, or by the doctrine of account stated, or by an estoppel.

I have found that the Libyan Bank did not in fact appreciate what was happening until mid-1985; but they could have detected earlier that they were not receiving the full benefit by way of interest to which they were entitled, if they had looked at their bank statements with a fair degree of diligence.

I am prepared to assume that New York law does govern this aspect of the relations between the parties, if and to the extent that I have not already held that it does.

Evidence of New York law on this topic was given by Professor Felsenfeld on behalf of the Libyan Bank and Mr. Knake on behalf of Bankers Trust. Professor Felsenfeld's opinion was that failure by the Libyan Bank to comment on the bank statements would not excuse Bankers Trust for an intentional, negligent or culpable act on their part; that Bankers Trust would have to establish that they relied on the conduct of the Libyan Bank and acted on it to their detriment; and that they could not disclaim responsibility for their own good faith or their duty to exercise ordinary care. There was not a great deal of dispute as to those propositions, and to the extent that there was I prefer the evidence of Professor Felsenfeld. But the real question here was as to the facts. The Professor was asked this question in re-examination:

"Suppose a bank goes to its customer and tries to alter the basis on which interest is charged so as to improve the return to the bank and the customer refuses to agree to the new

arrangement that the bank proposes, and that subsequently the bank introduces another arrangement in the hope that the customer won't spot it. Is the bank acting bona fide in that way, or not?"
and the Professor answered: "I think you have described a rather flagrant example of bad faith." Mr. Knake was not wholly prepared to accept that; but I am. He was asked this question by me at the conclusion of his evidence:
"I have just one question for you, Mr. Knake, and it is on that same topic. We have been talking about duty of care. For the present, although my view may be changed, I have difficulty in seeing how there was any lack of care on the part of Bankers Trust. It seems to me they acted with great care. It is more a case of deliberate and calculated breach. If that be right what is your view on the account stated argument?" (An agreed correction has been made to the transcript.)
Mr. Knake answered:
"If that were to be your Lordship's finding then I would agree that under those circumstances if in fact they were, that is, Libyan Arab Foreign Bank were deceived, then I would have to agree with that, the absence of an account stated under those circumstances."

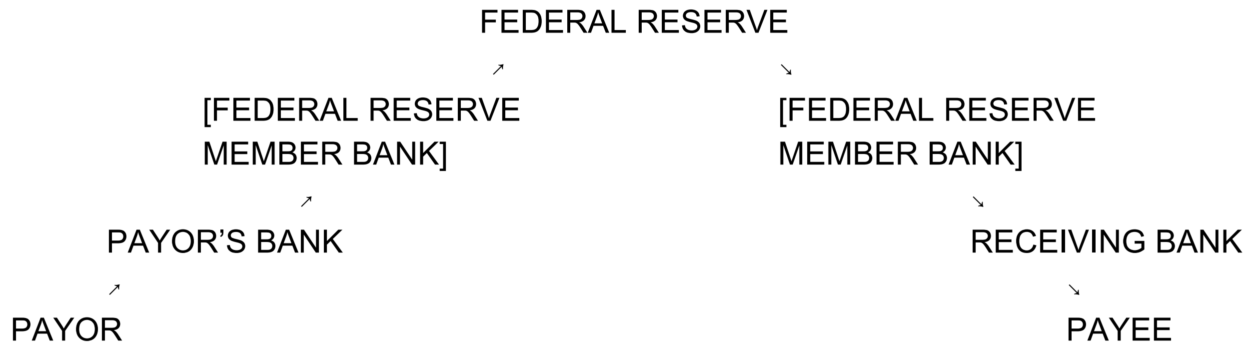
The facts as I have found them amount in substance to what was put to Professor Felsenfeld and Mr. Knake. Bankers Trust have no defence to this claim under New York law.

It is fair to add that in correspondence Bankers Trust alleged that they were only doing what other bankers habitually did. There was some modest support for that in the evidence of Mr. Blenk. But it has not been relied on before me as justification in law for the action of Bankers Trust.

The Libyan Bank are entitled to damages to be assessed in respect of this claim. There was mention in Mr. Cresswell's penultimate speech of another way of putting the claim - that on some days (other than 7 and 8 January) not even a 2 p.m. transfer was made when it should have been. I did not understand that to be one of the complaints on which the Libyan Bank came to court, and I have not considered or ruled upon it.

Conclusion
The Libyan Bank are entitled to recover U.S. $131m. on claim (1) and U.S. $161m. (the amount of their demand) on claim (2). Claims (3) and (4) fail. Claim (5) would have failed if it had been material. On claim (6) the Libyan Bank must have judgment for damages to be assessed.
Postscript
In August of this year there were 20 working days. Fourteen of them were entirely consumed in the preparation of this judgment. In those circumstances it is a shade disappointing to read in the press and elsewhere that High Court judges do no work at all in August or September and have excessively long holidays.

The decision suggests that there are a number of options for clearing US dollar payments. Fedwire is a real-time gross settlement system for settling payments in US dollars.[26] The payor instructs her bank to make the payment which must pass through the federal reserve system using banks which are members of that system. If the payor's bank and or payee's bank are not members they must involve correspondent banks which are members in the transaction.



CHIPS[27] is a real time net settlement system. In Fedwire all payments are made without taking account of other payments, so if Bank A must make $100 million payments to Bank B in any one day and Bank B must make $50 million payments to Bank A each transfers the gross amount. In a net system the participants may be able to transfer only the net amount. A net system has greater liquidity than a gross system, but may have greater risk, so CHIPS has complex systems for minimizing risk.

Should the illegality in the US have excused Bankers' Trust's failure to pay Libyan Arab Bank? What do you think of Staughton's split proper law? Why was Staughton so sceptical about some of the expert evidence?

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[26] See http://www.federalreserve.gov/paymentsystems/fedfunds_about.htm . Target is the real time gross settlement system for euro. You can find information on Target here: http://www.ecb.int/paym/html/index.en.html .

[27] *See* http://www.chips.org

RELATIONSHIPS BETWEEN BORROWERS AND LENDERS AND THE ARRANGER AND AGENT BANKS

Many of the provisions in the credit agreement govern the relations between the different participants.[28] Would you be happy with these provisions if you were: the agent; a lender; or the borrower? The interests of the different parties may conflict. The roles of arranging bank, or arranger, which structures the transaction, and of the agent bank which arranges for the transmission of moneys between the parties, may be performed by different entities or by the same entity.

Miguel Ferreira and Pedro Matos have examined relationships between bank connections to borrowing firms and the banks' taking on the role of arranger of syndicated loans: [29]

...firms tend to get more loans arranged by banks to which they are closely connected, relative to banks without connections to the firm. Banks with a board member in firms are 12% more likely to be picked as lead arrangers than unconnected banks, which is twice the average probability in the sample. This is a large economic magnitude as the base probability in our sample is that a bank has 10% probability of being chosen to provide a loan . Effects are also sizeable for the case where bank has institutional holdings (4% increase in probability) and even higher if the bank has a direct equity stake (25% increase in probability)...We also find that the effect of a bank-firm connection is stronger for firms with less alternative financing choices and those from countries with worse legal environments.
.We find that banks with board seats or with institutional holdings in the borrower firm charge a higher interest rate spread relative to banks without connections to the firm. The effects are also economically significant; the presence of a bank member in the firm's board of directors is associated with a higher spread charged to the firm of about 8 basis points (and 15 basis points for the case of bank institutional holdings).... This finding suggests that banks are able to "capture" the firm when they play a role in the corporate governance of the firm....
These effects on loan pricing are consistent with the "information rent extraction" hypothesis, i.e. the information advantage of the insider bank may deter competition from other banks or create a lemons problem in that other banks will be skeptical of the quality of firm that do not

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[28] If you want to read further on this issue you could look at Gavin R. Skene, *Arranger Fees in Syndicated Loans - A Duty to Account to Participant Banks?*, 24 PENN ST. INT'L L. REV. 59 (2005).

[29] Miguel A. Ferreira & Pedro Matos, When Banks are Insiders: Evidence from the Global Syndicated Loan Market (Sept. 2008). A version of this paper was published as Miguel A. Ferreira & Pedro Matos, Universal Banks and Corporate Control Evidence from the Global Syndicated Loan Market, European Central Bank, Working Paper no 1066 (Jul. 2009) at http://www.ecb.int/pub/pdf/scpwps/ecbwp1066.pdf .

use their universal bank as lead arranger .... We also find that bank -firms connections tend to increase lender concentration, i.e. connections have a negative and significant effect on the number of lead arrangers and lenders used by the borrower firm.
Finally, we investigate the ex-post performance of firms that borrow in the syndicated loan market. We ask the question whether firms that get loans from connected banks have less ex-post credit risk. We find that the existence of a bank-firm connection at the time of the loan initiation is associated with a decrease in the expected default probability (EDF from Moody's KMV) in the year following the loan initiation. Therefore, banks with connections seem to benefit from an improvement in the credit quality of the firms they lend to as compared to banks with no connections. This evidence is suggestive that insider banks access private information of good financial status of the borrower.

In the US, three banks (J.P. Morgan Chase, Bank of America, and Citigroup) dominate the syndicated loan market:

The dominant banks, it would seem, have a commanding market share because they have a particularly high—and possibly selfreinforcing— reputation for screening and monitoring. The results also suggest that the dominant banks have an advantage in distribution, allowing them to offer loans at a lower all-in cost, even to borrowers with an established reputation in the credit markets.[30]

Participation in syndicated loan arrangements may have an impact on the participants beyond the loan itself:

Although the study of inter-bank relationships over the past decade has documented some of the benefits and costs of temporary alliances (such as loan syndications), much remains unknown. For instance, do financial institutions consider syndicated loans as pure business transactions, or do they also benefit from their relational nature in other ways? What are the effects and consequences of alliances formed through banking syndicates? Specifically, do these alliances lead to more formal alliances between syndicate participants, such as M&As? Do the M&As involving parties with previous syndicate co-alliances perform better than those without such previous co-alliances?...
The probability of an M&A between two lenders increases significantly when the institutions partnered in the five-year period before the M&A and the odds of a merger are higher for every percent increase in the relative importance of the past alliances. The impact of past

[30] David Gaddis Ross, The "Dominant Bank Effect:" How High Lender Reputation Affects the Information Content and Terms of Bank Loans 23 (7) Rev. Financ. Stud. 2730, 2754 (2010).

relationships between the acquirer and the target is stronger for international alliances and cross-industry mergers as well as for cases where the acquirer and target are participant and lead, respectively, in these past alliances.[31]

Does the Arranger/ Agent bank/ a lender owe fiduciary duties to the borrower?

A bank which obtains confidential information about a firm may be precluded from using that information for its own benefit. In **United Pan-Europe Communications NV v Deutsche Bank AG**[32] UPC complained that DB had used confidential information it had acquired as a participant in syndicated loans to UPC in formulating a bid to acquire another firm (in competition with UPC). The following brief excerpt is from Lord Justice Morritt's judgment in the Court of Appeals :

37. The fiduciary duty is alleged to have arisen from the key banking relationship formerly existing between UPC and DB, the mutual trust and confidence without which it could not properly operate and the requirement duly performed that UPC pass to DB confidential information of the type referred to on a regular basis. The amended points of claim also allege a contractual duty and a duty to the like effect to be implied from established banking practice in both England and Germany. Before us no reliance was placed on the contractual duty as it would not give rise to the proprietary remedy sought. We have not seen any evidence of banking practice. ...
38. Both parties agreed that the relevant law was to be found in the judgment of Millett LJ in Bristol and West Building Society v Mothew [1996] 4 All ER 698 at 711-712... (approved by the Privy Council in Arklow Investments Ltd v Maclean [2000] 1 WLR 594 at 599):
'A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations. They are the

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[31] Claudia Champagne & Lawrence Kryzanowski, *The Impact of Past Syndicate Alliances on the Consolidation of Financial Institutions*, 37 (3) Financial Management 535, 536, 566 (2008).

[32] [2000] 2 BCLC 461

defining characteristics of the fiduciary. As Dr Finn pointed out in his classic work Fiduciary Obligations (1977) p.2, he is not subject to fiduciary obligations because he is a fiduciary; it is because he is subject to them that he is a fiduciary.'

39. In this respect Jacob J considered (para 17) that:

'In Arklow Investments Ltd v Maclean [2000] 1 WLR 594, because the defendants had not undertaken the job, it was held that they had never become fiduciaries. [Counsel for UPC] submitted that the facts of this case were otherwise because DB had undertaken tasks for UPC. Thus the law did make them fiduciaries. As I have said I am not convinced that the present evidence would justify such a conclusion in relation to anything to do with TeleColumbus. No doubt DB would be fiduciaries in relation to the matters undertaken. What is really at stake here is the width of those fiduciary obligations and, in particular, whether they extend well beyond those tasks. As I say that will involve a fuller investigation of those tasks and of banking practice."

40. In this passage the judge recognises, and I agree, that DB was under some fiduciary duty to UPC the scope of which could only be determined at the trial. A similar problem arose in New Zealand Netherlands Society 'Oranje' Inc v Kuys [1973] 2 All ER 1222 ...The question was whether the conduct complained of came within the scope of the defendant's fiduciary duty as an officer of the society... Lord Wilberforce noted that a person in the position of Kuys might be in a fiduciary position quoad a part of his activities and not quoad other parts, 'each transaction, or group of transactions, must be looked at'. He approved as a principle of general application the statement of Dixon J in Birtchnell v Equity Trustees, Executors and Agency Co Ltd (1929) 42 CLR 384 at 408 that:

'The subject matter over which the fiduciary obligations extend is determined by the character of the venture or undertaking for which the partnership exists, and this is to be ascertained, not merely from the express agreement of the parties . . . but also from the course of dealing actually pursued by the firm.'

41. As I understood him counsel for DB did not disagree. He accepted that, for example, having lent money to UPC for the acquisition by UPC of Telekabel NV, DB was precluded from then bidding for Telekabel NV in competition with UPC. Thus the issue is not the existence of the fiduciary duty but of its scope. That issue is one that is largely dependent on the facts and cannot be resolved at this stage. Accordingly in my view the court must approach this application on the footing that there is a seriously arguable case for breach of fiduciary duty as well as misuse of confidential information.

Cases in the US have suggested different views about whether investment banks were subject to fiduciary duties (and this is not surprising as whether or not fiduciary duties arise depends on the circumstances, and even where fiduciary duties do apply the content of the duties also depends on the circumstances).

In **EBCI Inc v Goldman Sachs**[33] the New York Court of Appeals found that claims that Goldman Sachs had breached fiduciary duties as an underwriter of a securities offering survived a motion to dismiss:

Goldman Sachs argues that the relationship between an issuer and underwriter is an arms-length commercial relation from which fiduciary duties may not arise. It may well be true that the underwriting contract, in which Goldman Sachs agreed to buy shares and resell them, did not in itself create any fiduciary duty. However, a cause of action for breach of fiduciary duty may survive, for pleading purposes, where the complaining party sets forth allegations that, apart from the terms of the contract, the underwriter and issuer created a relationship of higher trust than would arise from the underwriting agreement alone.
Here, the complaint alleges an advisory relationship that was independent of the underwriting agreement. Specifically, plaintiff alleges eToys was induced to and did repose confidence in Goldman Sachs's knowledge and expertise to advise it as to a fair IPO price and engage in honest dealings with eToy's best interest in mind. Essentially, according to the complaint, eToys hired Goldman Sachs to give it advice for the benefit of the company, and Goldman Sachs thereby had a fiduciary obligation to disclose any conflict of interest concerning the pricing of the IPO. Goldman Sachs breached this duty by allegedly concealing from eToys its divided loyalty arising from its profit-sharing arrangements with clients.
Contrary to Goldman Sachs's contention, recognition of a fiduciary duty to this limited extent -- requiring disclosure of Goldman Sachs's compensation arrangements with its customers - - is not in conflict with an underwriter's general duty to investors under the Securities Act of 1933 to exercise due diligence in the preparation of a registration statement... An obligation not to conceal from the issuer private arrangements made with a group of potential investors does not compromise Goldman Sachs's charge to be truthful in its public disclosure regarding the issuer's business. For similar reasons, we do not share the dissent's concern that upholding an issuer's fiduciary duty claim against an underwriter "potentially conflicts with a highly complex regulatory framework designed to safeguard investors" ... Recognizing a common law remedy, under these circumstances, will not hinder the efforts being expended to regulate in this area.... Goldman Sachs warns that to find a fiduciary relationship in this case may have a significant impact on the underwriting industry. We think its concern is overstated. To the extent that underwriters function, among other things, as expert advisors to their clients on market conditions, a fiduciary duty may exist. We stress, however, that the fiduciary duty we recognize is limited to the underwriter's role as advisor. We do not suggest that underwriters are fiduciaries when they are engaged in activities other than rendering expert advice. When they do render such advice, the requirement to disclose to the issuers any material conflicts of

[33] 5 N.Y.3d 11; 832 N.E.2d 26; 799 N.Y.S.2d 170 (2005).

interest that render the advice suspect should not burden them unduly.
Accepting the complaint's allegations as true, as the Court must at this stage, plaintiff has sufficiently stated a claim for breach of fiduciary duty. This holding is not at odds with the general rule that fiduciary obligations do not exist between commercial parties operating at arms' length -- even sophisticated counseled parties -- and we intend no damage to that principle. Under the complaint here, however, the parties are alleged to have created their own relationship of higher trust beyond that which arises from the underwriting agreement alone, which required Goldman Sachs to deal honestly with eToys and disclose its conflict of interest -- the alleged profitsharing arrangement with prospective investors in the IPO.

Judge Read, dissenting, said:

This new fiduciary obligation wars against our precedent and potentially conflicts with a highly complex regulatory framework designed to safeguard investors...we have..until today.. refrained from injecting fiduciary obligations into sophisticated, counseled parties' arm's length commercial dealings. In refusing to fashion a "newly-notched fiduciary-like duty" for finders in Northeast Gen. Corp. v Wellington Adv. (82 NY2d 158, 161 [1993]), we remarked that "[i]f the parties find themselves or place themselves in the milieu of the 'workaday' mundane marketplace, and if they do not create their own relationship of higher trust, courts should not ordinarily transport them to the higher realm of relationship and fashion the stricter duty for them."...In allowing plaintiff's claim for breach of fiduciary duty to go forward, the majority disregards that eToys was a sophisticated, well-counseled business entity... Further, the offering price was a key term in the underwriting agreement, a purchase contract between eToys, the issuer/seller, and Goldman, the underwriter/buyer, who represented all the underwriters in the syndicate. How may a buyer ever owe a duty of the highest trust and confidence to a seller regarding a negotiated purchase price? The interests of a buyer and seller are inevitably not the same. Indeed, it is a longstanding principle of contract law that a buyer may make a binding contract to buy something that it knows its seller undervalues... Here, eToys' prospectus acknowledged that the "initial public offering price for the common stock has been negotiated among eToys and the representatives of the underwriters" (emphasis added). Contrary to plaintiff's allegation, eToys also represented in the prospectus that the offering price was not driven by anticipated demand alone. The other factors that came into play were "eToys' historical performance, estimates of eToys' business potential and earnings prospects, an assessment of eToys' management and the consideration of the above factors in relation to market valuation of companies in related businesses." Further, eToys' prospectus identified four "principal purposes" for the IPO: to increase working capital, create a public market for its stock, facilitate future access to the public capital markets, and increase visibility in the retail marketplace. By selling only 8.2% of its outstanding common stock at $20 a share, eToys raised the capital called for by its business plan.

In short, the offering price was not "set" by Goldman, it was negotiated by sophisticated, represented parties—the issuer/seller and the underwriter/buyer; the offering price was negotiated with reference to more than "then current market conditions" and "anticipated demand"; and eToys did not seek to negotiate an offering price solely to maximize the proceeds raised in the offering. Documentary evidence in the record confirms all these points, and the nature of the contractual relationship between an issuer and an underwriter is long-established and well-understood...

How our new fiduciary duty for underwriters may fit into or conflict with the developing regulatory scheme is impossible to predict. We have, however, at the very least introduced uncertainty into a complex subject of enormous importance to investors. This subject is, in my view, better dealt with by specialized regulators than by the evolving common law..

The Loan Syndications and Trading Association (LSTA) expressed concern about this decision:

This opinion is of potential concern to the loan market for a number of reasons. For the first time, the highest New York court has, as the dissent argued, injected "fiduciary obligations into sophisticated, counseled parties' arms-length commercial dealings." Although this decision applied to a securities underwriting, it was based on New York common law, not federal or state securities statutes, and therefore could potentially apply equally to the relationship between borrowers and underwriters of large corporate loans. It is particularly relevant because New York law is frequently chosen as the governing law for large syndicated corporate loans.

In light of the Court of Appeal's decision, underwriters of syndicated corporate loans may seek to protect themselves against a borrower's claim of breach of fiduciary duty by expressly disclaiming any fiduciary duties as advisor or otherwise. These disclaimers should be included at the outset in engagement and commitment letters that govern the parties' relationships, and should make clear that the underwriter will not assume any fiduciary duties.

In **HF Management Services LLC v. Pistone**, [34] the New York Appellate Division emphasized that the Court of Appeals in the Goldman Sachs case had said that the underwriter/issuer relationship is not usually a fiduciary relationship:

In the case at bar, nothing in the record even remotely suggests that the relationship between Morgan Stanley and WellCare rose above the typical contractual relationship of an underwriting agreement between a buyer and a seller. Both parties were separately counseled. In fact, the underwriting agreement specifically identified EBG as the "special regulatory counsel for the

[34] http://www.courts.state.ny.us/REPORTER/3dseries/2006/2006_05153.htm

underwriters" and acknowledged that another law firm was serving as outside counsel for WellCare. Certainly, there is no indication or suggestion that Morgan and WellCare enjoyed any type of pre-existing relationship, or that Morgan acted as an "expert advisor on market conditions" to WellCare in the same way that Goldman Sachs apparently advised eToys..

In 2008, the 7th Circuit held in **Joyce v Morgan Stanley** [35] that the bank which had issued a fairness opinion with respect to a merger did not have a fiduciary duty to shareholders to advise them to hedge the shares:

...we see no way that the Shareholders can show that their relationship with Morgan Stanley possessed the “special circumstances” necessary to give rise to an extra-contractual fiduciary duty. One such necessary “circumstance” is that the allegedly superior party must have accepted a duty to guard the interests of the dependent party. Pommier v. Peoples Bank Marycrest, 967 F.2d 1115, 1119 (7th Cir. 1992) (“The fact that one party trusts the other is insufficient. We trust most people with whom we choose to do business.The dominant party must accept the responsibility, accept the trust of the other party before a court can find a fiduciary relationship.”)...
The exhibits leave no doubt that Morgan Stanley did not accept any such responsibility, and so no fiduciary duty toward the Shareholders ever arose. The engagement letter, which defines the advising relationship, explicitly noted that Morgan Stanley was working only for the corporation: “Morgan Stanley will act under this letter agreement as an independent contractor with duties solely to 21st Century.” ... “We have acted as financial advisor to the Company in connection with this transaction . . . .” ...
The fairness opinion also disclaimed a duty to the Shareholders:
It is understood that this letter is for the information of the Board of Directors of the Company, except that this opinion may be included in its entirety in any filing required to be made by the Company in respect of the Merger. Morgan Stanley expresses no opinion as to the relative valuations of each of the voting and non-voting 21st Century Common Stock and the 21st Century Preferred Stock. In addition, this opinion does not in any manner address the prices at which the RCN Common Stock will trade following announcement or consummation of the proposed Merger, and Morgan Stanley expresses no opinion or recommendation as to how the holders of the 21st Century Common Stock should vote at the shareholders’ meetings held in connection with the Merger....
Thus, Morgan Stanley never owed any contractual nor extra-contractual duty to the Shareholders.

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35 http://www.jdsupra.com/post/fileServer.aspx?fName=dcd15bea-e309-4cb8-8e8b-82ccca466d2a_searchable.pdf

Does the Arranger/ Agent bank owe fiduciary or other duties to the lenders?

The loan agreement will seek to limit obligations of the arranger in different ways. One set of limitations focuses on the obligation of the lenders to make their own credit assessments. In general courts are likely to uphold these provisions. In **Bank of the West v Valley National Bank of Arizona**, 41 F.3d 471 (1994) a case arising out of a loan participation the 9th Circuit said this:

...Valley National acted as though the relationship was that of a lead bank doing all the investigation and exercising all the judgment, and the participating bank passively investing in the lead bank's lending program. Valley National's problem is that regardless of what they actually did, the banks expressly agreed to a relationship in which each would investigate independently and exercise independent judgment. There was no lack of clarity in the contract, no mutual mistake, no reason to suppose that the parties mutually intended any relationship other than what the contract said. The loan participation agreement expressly provided that the Bank of the West "does not assume and shall have no responsibility or liability" for Technical Equities' financial condition, the collateral, or collectibility of the loan. Valley National agreed that it "independently and without reliance upon any representations of Lender . . . made and relied upon [its] own credit analysis and judgment." Valley National promised to "continue to make and rely upon" its own decisions "independently and without reliance upon" Bank of the West.

Those are plain and strong words. The most favorable characterization of Valley National's conduct which the evidence allows is that it promised not to rely on Bank of the West, but then did in fact rely on Bank of the West. That necessarily implies that, to the extent that it did rely on Bank of the West, Valley National's reliance was not justifiable.

The contract could as a practical matter only control litigation outcomes, not conduct. Valley National might choose to advance millions of dollars without making an independent credit evaluation, in reliance on Bank of the West's judgment, even though it promised not to do that. That might be a rational business judgment, if experience with Bank of the West had always been very good, Technical Equities looked good, and an independent evaluation would cost more money than the value of the risk which it would likely avert. But the contract could and did control whether such reliance would be "justifiable" for purposes of a fraud claim...

Other provisions limit the liability of an agent bank in relation to various aspects of the loan relationship:

Chemical Bank v Security Pacific National Bank[36]

That Security Pacific owed a fiduciary duty to the plaintiffs is established by the credit agreement of April 8, 1983 which unequivocally identifies Security Pacific as the agent bank. The very meaning of being an agent is assuming fiduciary duties to one's principal. Restatement (Second) of Agency § 1(1). The holding of this court in First Citizens Federal Savings and Loan Association v. Worthen Bank and Trust Co., 919 F.2d 510 (9th Cir. 1990), which requires "unequivocal contractual language" to create a fiduciary duty, is not to the contrary. In that case the bank was the principal lender and was identified as "an independent contractor." Id. at 512, 514. There was no intention on the part of this court to abandon "the special concern common law courts have traditionally and consistently exhibited to supervise and enforce fiduciary relationships," including the fiduciary relationship when one bank acts as the agent for another bank. Women's Federal Savings and Loan Association v. Nevada National Bank, 811 F.2d 1255, 1258 (9th Cir. 1987).

Impressed with a fiduciary responsibility, Security Pacific failed to carry it out. Beyond question, it breached its duty and its contract. Beyond question it acted negligently. But there is no law against parties to a contract relieving themselves of liability by contract, particularly when they are sophisticated institutions represented by knowledgeable counsel. The credit agreement that all three banks signed went a long ways toward relieving Security Pacific of what it might otherwise have been expected to do. It was explicitly not required to "be responsible in any manner" for the "enforceability" of the credit agreement. According to the credit agreement, it was liable only for its "own gross negligence or willful misconduct."....

It is, no doubt, odd that three sophisticated lending institutions would enter into an agreement with themselves that puts the responsibility on their agent in such a doubtful state that lay persons, chosen more or less at random, are to be the ones to determine whether the responsibility was met. But if these banks chose to operate their business in this way, it is not the court's function to provide a judge to determine a question that properly belongs to a trier of fact.

The context is significant. **Courts are likely to be less willing to decide that fiduciary duties arise in the context of arm's length commercial transactions between sophisticated parties than in other cases. Do you think that this is the right approach?**

[36] 20 F.3d 375 (9th Cir 1994)

Gavin Skene, an Australian lawyer, has written:[37]

The complex relationships formed between the arranger, the borrower and the participant banks under a syndicated loan exposes the arranger to considerable legal risk. The nature of the role assumed by the arranger under these relationships is often competing and adverse to the interests of each other party, including the arranger's own self interests, under the syndicated loan.

This position is especially true where an arranger has also been appointed as agent bank under a syndicated loan because its duties and obligations will "shift" primarily from the borrower and possibly the participant banks to just the participant banks when one role ceases and the other commences. Accordingly, there may be circumstances where it is unclear as to whom the arranger owes certain duties, the length of time that the duties are owed, or whether such duties have merged....

Modern courts of common law jurisdictions have wrangled generally with the expansion of the law of equity into the province of commerce. The inherent incompatibility between equity, which promotes fairness and justice on the one hand, and commerce, which protects self-advancement and self-promotion on the other, can be clearly illustrated in the case of the invocation by a court of a fiduciary relationship between an arranger and the participant banks under a syndicated loan.

It is generally accepted that the relationship between an arranger and a participant bank falls outside the boundaries of the established fiduciary relationship categories. Therefore, an Australian court must have regard to the relevant jurisprudence relating to the intrusion of the fiduciary relationship into commercial transactions when considering whether or not the character of the relationship between an arranger and participant bank is one that exhibits the necessary characteristics present in a fiduciary relationship.

Given the size and volume of syndicated loans made in the global marketplace each year, it is surprising that there is little authoritative case law in common law jurisdictions that examines the set of legal relationships between the actors of a syndicated loan generally and the legal rights and obligations that flow between an arranger and the participant banks specifically....

...arrangers of syndicated loans should be mindful that if it is determined that the benefit to any arranger fees was enjoyed by an arranger in its capacity as agent bank and not as arranger of a syndicated loan, there is a risk that the said arranger will owe equitable duties to account to the participant banks for the receipt of such arranger fees procured in its capacity as agent for the participant banks.

In **Sumitomo Bank Ltd v Banque Bruxelles Lambert SA** [1997] 1 Lloyd's Rep 487

[37] See note 28 above.

(QBD, Langley J.), the court found that the fact that BBL owed limited duties as agent under the loan agreement did not prevent a wider duty of care from arising out of the relationship between the parties. In this case the loans were to finance the purchase of commercial property, and there were mortgage indemnity guaranty policies (MIGs) underwritten by Eagle Star which would protect the banks against losses if the borrower defaulted on the loans. After default Eagle Star argued that the MIGs were void for non-disclosure. The banks argued that BBL as arranger of the loans had a duty to ensure that the borrower performed its disclosure obligations under the MIGs. BBL argued that the terms of the loan agreement were inconsistent with the duty of care, implied terms and fiduciary duties that the banks were arguing for. BBL also argued that there was a clear market practice that unless there was a specific written warranty or assurance an arranging bank did not owe duties to participating banks. Consider the following excerpt from the judgment:

(2) Duty of care

Two basic approaches to the question whether in a given case a duty of care arises can be discerned from the leading authorities. The first can be summarized in the familiar rubric of foreseeability, proximity, and whether the imposition of a duty of care would be fair, just and reasonable. The second can be summarized in the words "voluntary assumption of responsibility". In this case, I do not think it matters which approach is taken as in my judgment the result is the same on either basis but I will set out what I think to be the major statements of principle supporting the two approaches.

First, Caparo Industries Plc v Dickman, [1990] 2 AC 605. I need not state the facts. The principles are to be found in the speeches of Lord Bridge at pp 620-621 and Lord Oliver at p 638.

Lord Bridge said:

> The salient feature of all these cases (cases where a duty of care had been held to arise) is that the defendant giving advice or information was fully aware of the nature of the transaction which the plaintiff had in contemplation, knew that the advice or information would be communicated to him directly or indirectly and knew that it was very likely that the plaintiff would rely on that advice or information in deciding whether or not to engage in the transaction in contemplation. In these circumstances the defendant could clearly be expected, subject always to any disclaimer of responsibility, specifically to anticipate that the plaintiff would rely on the advice or information given by the defendant for the very purpose for which he did in the event rely on it. So also the plaintiff, subject again to the effect of any disclaimer, would in that situation reasonably suppose that he was entitled to rely on that advice or information communicated to him for

> the very purpose for which he required it. The situation is entirely different where a statement is put into more or less general circulation and may foreseeably be relied on by strangers to the maker of the statement for any one of a variety of different purposes which the maker of the statement has no specific reason to anticipate.

Lord Oliver said:

> What can be deduced from the Hedley Byrne case, therefore, is that the necessary relationship between the maker of a statement or giver of advice ("the adviser") and the recipient who acts upon it ("the advisee") may typically by held to exist where (1) the advice is required for a purpose, whether particularly specified or generally described, which is made known, either actually or inferentially, to the adviser at the time when the advice is given; (2) the adviser knows, either actually or inferentially, that his advice will be communicated to the advisee, either specifically or as a member of an ascertainable class, in order that it should be used by the advisee for that purpose; (3) it is known either actually or inferentially, that the advice so communicated is likely to be acted upon by the advisee for that purpose without independent enquiry, and (4) it is so acted upon by the advisee to his detriment.

Second, the approach in Henderson v Merrett Syndicates Ltd, [1994] 2 Lloyd's Rep 468; [1995] 2 AC 145 namely, whether it can be said that the defendant voluntarily assumed or undertook responsibility to the plaintiff in respect of the subject-matter of the representation. After an analysis of the speeches in Hedley Byrne, Lord Goff at pp 488-489; pp 180-181 said:
From these statements, and from their application in Hedley Byrne, we can derive some understanding of the breadth of the principle underlying the case. We can see that it rests upon a relationship between the parties, which may be general or specific to the particular transaction, and which may or may not be contractual in nature. All of their Lordships spoke in terms of one party having assumed or undertaken responsibility towards the other . . . Again though Hedley Byrne was concerned with the provision of information and advice, the example given by Lord Devlin of the relationship between solicitor and client, and his and Lord Morris's statement of principle, show that the principle extends beyond the provision of information and advice to include the performance of other services. It follows, of course, that although, in the case of the provision of information and advice, reliance upon it by the other party will be necessary to establish a cause of action (because otherwise the negligence will have no causative effect), nevertheless there may be other circumstances in which there will be the necessary reliance to give rise to the application of the principle. In particular, as cases concerned with solicitors and client demonstrate, where the plaintiff entrusts the defendant with the conduct of his affairs, in general or in particular, he may be held to have relied on the defendant to exercise due skill and care in such conduct.
. . . Furthermore, especially in a context concerned with a liability which may arise under a

contract or in a situation "equivalent to contract", it must be expected that an objective test will be applied when asking the question whether, in a particular case, responsibility should be held to have been assumed by the defendant to the plaintiff: See Caparo per Lord Oliver.

Lord Goff also addressed the relevance of the contractual context to the principles he had stated. He held that in principle the existence of concurrent remedies in contract and tort was established in law and that (at p 498, col 1; p 194):

. . . an assumption of responsibility coupled with the concomitant reliance may give rise to a tortious duty of care irrespective of whether there is a contractual relationship between the parties, and in consequence unless his contract precludes him from doing so, the plaintiff who has available to him concurrent remedies in contract and tort may choose that remedy which appears to him to be the most advantageous.

Those words must, in my judgment, apply a fortiori to circumstances where the relevant relationship and assumption of responsibility arises (if it arises) before the contract comes into existence and the relevant duty in tort should in practical terms have been performed at the time the contract was concluded. That was the position as regards the obligation of disclosure in this case and, moreover, as I have held, the relevant contract, namely the loan agreement, was not addressing that obligation nor inconsistent with it.

That this is so is further illustrated by the unreported decision of the Court of Appeal in Holt v Payne Skillington and De Groot Collis, Dec 18,1995. That decision demonstrates that a duty of care can be owed in tort which is more extensive than the express or implied obligations to be derived from the terms of the contract made between the same parties. Lord Justice Hirst in giving the judgment of the Court said (at p 15), after referring to the passage from the speech of Lord Goff in Henderson v Merrett to which I have referred:

. . . as Lord Goff made clear . . . it will frequently be the case that the relevant assumption of responsibility does occur within a contractual context. That fact does not mean that it must necessarily do so simply because, at some stage during the relevant course of dealing between the parties, they choose to and do enter into some form of contract. A consideration of the individual facts and circumstances of each case will determine whether any duty of care in tort which the general law may impose is of wider scope than any contract to which the same parties may agree at some stage during the same course of dealing. It is important to emphasise that the duty of care in tort is, in appropriate circumstances, imposed by the general law, whereas the contractual obligations result from the common intentions of the parties. In our opinion, there is no reason in principle why a Hedley Byrne type duty of care cannot arise in an overall set of circumstances where, by reference to certain limited aspects of those circumstances, the same parties enter into a contractual relationship involving more limited obligations than those imposed by the duty of care in tort. In such circumstances, the duty of care in tort and the duties imposed by the contract will be concurrent but not coextensive. The difference in scope between the two will reflect the more limited factual basis which gave rise to the contract and the absence of any term in that contract which precludes or restricts the wider

duty of care in tort.

Those words, in my judgment, apply here where the loan agreement established and looked forward to the role of BBL as agent bank but did not relate to or look back to their role as arranging bank prior to the agreement.

BBL was putting together the transactions and had an interest in getting the banks to participate in them and indeed was being rewarded for that role. Mr Fraser himself readily acknowledged that the MIGs were for each of the banks a key part of the transaction and that he knew at the time that if BBL did not comply with the disclosure obligation in the policies Eagle Star could avoid the policies which would have the consequence for each of the banks that they would be unable to enforce them. MrFraser agreed that it would also have been obvious to the banks that that was so. While asserting his belief that the duty of disclosure rested on each of the banks he said he thought each of the banks, including BBL, had a duty of care "on one another" in effect to avoid that consequence. He agreed that the banks could not know or verify whether BBL had complied with the disclosure obligation and that each of the banks in each transaction relied on BBL to perform that obligation and he knew at the time that they did so. In addition it was his view, as it was the view of the banks, that the disclosure obligation was not an exceptional or onerous one and of course not only had it been negotiated by BBL but it was no greater than the "obligation" BBL in effect owed to itself in its own interests to establish the efficacy of the policy. The fact that Mr Fraser or BBL may have believed that the arrangements were "non-recourse" is in these circumstances of no materiality. That was not communicated to the banks and the test of duty is objective.

On the other side, the banks had to rely on BBL performing the disclosure obligation as it was (as I have held) tailored to BBL's own procedures. Each bank expected and relied on BBL to perform the obligation and believed it would and indeed, and understandably, hardly contemplated that it would not do so. That expectation and reliance was in my judgment entirely reasonable.

In these circumstances I think the relationship between BBL and the plaintiff banks was, to use the words of Lord Goff in Henderson v Merrett, a "classic example" of a relationship where a duty of care did arise on BBL to the banks as regards the performance of the disclosure obligations under the MIGs.

There was an assumption of responsibility by BBL to the banks to perform that duty. BBL was "the arranger" of the facility. It assumed as such the obligation to negotiate and agree the MIGs with Eagle Star. It did so on terms whereby, as I have held, it and it alone was the insured under the policy and it and it alone had and could perform the disclosure obligation provided for in it which depended on its own expert procedures and its skill and judgment in deciding what should be disclosed to Eagle Star. BBL knew the validity of the policies depended on its proper performance of that obligation. It knew the policies were vital to the interests both of itself and the banks and that the banks were dependent upon it for the performance of the disclosure obligation which effectively was entrusted to it in all their interests. The banks relied on BBL

accordingly as BBL knew they would. Loss to the banks if the duty was not performed was foreseeable and indeed foreseen by BBL. The duty arose in the context of the specific purpose of the loan transactions. Nor, for the reasons I have given, do I think the existence of a duty of care does any violence to or is in any way inconsistent with any market practice or the provisions of the loan agreements.
For these reasons in my judgment, and whether one approaches the matter by way of Caparo or Henderson v Merrett, the answer is the same. BBL owed the plaintiff banks a duty of care in carrying out the disclosure obligation under the policies in relation to both the Cornlease and Bridgecirc transactions.

Is the judge in Sumitomo v BBL generally just unfriendly to the idea of a limitation of liability, or do you think that BBL could have effectively protected itself against liability in this case? Why did it not do so?

IFE Fund SA v Goldman Sachs International[38] seems to suggest that the Sumitomo case must be read narrowly and to apply only to its specific facts. In IFE v Goldman Sachs, the English Court of Appeal considered the effect of a notice which limited Goldman Sachs' (GSI's) responsibilities with respect to information contained in a Syndication Information Memorandum (SIM) for the issuance of debt securities. Lord Justice Waller's judgment contains the language of the notice:

13 By its defence GSI also relied on the terms of the "Important Notice" under cover of which the SIM was provided to IFE and all possible participants. That notice contained standard terms under which arrangers and underwriters in the world of syndicated finance provide SIMs. Indeed as explored in some detail in cross-examination, they are the standard terms adopted by IFE when it acts as arranger or underwriter. The important terms are the following, numbered for convenience:-

"(i) The information contained in this Memorandum has been obtained from the Sponsors, Autodistribution, Finelist, professional consultants and/or public sources. The Sponsors have approved the information obtained from them and its inclusion in this Memorandum, and have authorised the distribution of this Memorandum. None of this Memorandum, the information contained in it or any other information supplied in connection with the Facilities shall form the basis of any contract. Any future prospective co-underwriter or participant in the Facilities will be required to acknowledge in the Facilities contract that it has not relied on, or been induced to enter such agreement by, any representation or warranty, save as expressly set out in such agreement.

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[38] [2007] EWCA Civ 811 and at http://www.bailii.org/ew/cases/EWCA/Civ/2007/811.html .

(ii) The Arranger has not independently verified the information set out in this Memorandum. Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility is accepted by Goldman Sachs International, nor any of their holding companies, subsidiaries, associated undertakings or controlling persons, nor any of their respective directors, officers, partners, employees, agents, representatives or advisors as to or in relation to the accuracy or completeness or otherwise of this Memorandum or as to the reasonableness of any assumption contained therein or any other information made available in connection with the Facilities (whether in writing or orally) to any interested party (or its advisers). These disclaimers by the Arranger shall, for the avoidance of doubt, apply (without limitation) to the Valuation and Exit Strategy in Section IX of the Memorandum. Neither the Arranger nor any of its respective directors, officers, employees, agents, partners or professional advisers shall be liable for any direct, indirect or consequential loss or damage suffered by any person as a result of relying on any statement contained in this Memorandum or any such other information.

(iii) The information contained in this Memorandum should not be assumed to have been updated at any time subsequent to the date shown on the cover hereof and the distribution of this Memorandum does not constitute a representation by any person that such information will be updated at any time after the date of this memorandum. The Arranger expressly does not undertake to review the financial condition, status or affairs of Autodistribution, Finelist or any of their affiliates or any obligor in respect of the facilities, at any time or to advise any potential or actual participant in the Facilities of any information coming to the attention of the Arranger.

Lord Justice Waller wrote:

26. IFE have at all times made clear that they are not alleging dishonesty against GSI. Mr Howard for GSI has on the other hand from GSI's side made clear that he does not argue that the standard terms would allow GSI to act dishonestly. It was no doubt this concession which lead the judge to say what he did about an implied representation as to good faith...

27. As debate before us illustrated it is not that easy to define "dishonesty" or what might or might not be "in good faith" in a vacuum. Until one has identified what, if any, representations were being made or what duty of disclosure was owed one cannot really say what would or would not be honest or in bad faith. Furthermore if the decision were to be that there was a duty to disclose by virtue of what GSI had set out in the SIM, but GSI were honestly not aware of that duty, then their conduct might not as I would see it be dishonest...

28. I can start by clearing one or two issues out of the way. First it seems to me that the argument that there was some free standing duty of care owed by GSI to IFE in this case is in the light of the terms of the Important Notice hopeless. Nothing could be clearer than that GSI were not assuming any responsibility to the participants: Hedley Byrne v Heller & Partners [1964] A.C. 465. The foundation for liability for negligent misstatements demonstrates that where the terms on which someone is prepared to give advice or make a statement negatives

any assumption of responsibility, no duty of care will be owed. Although there might be cases where the law would impose a duty by virtue of a particular state of facts despite an attempt not "to assume responsibility" the relationship between GSI either as arranger or as vendor would not be one of them.

In the same case, Lord Justice Gage wrote:

67. For my part, I accept.. that the question of what representation, if any, was made by Goldman Sachs, must be considered by reference to the terms of the Important Notice in the SIM. The Notice expressly states that Goldman Sachs have not independently verified the information set out in it. It also states that it accepts no responsibility for the accuracy or completeness of the information contained in it. It must inevitably follow that no representation is made as to the accuracy or completeness of the Arthur Andersen reports of December 1999 and February 2000.
68 In my view, the third cited paragraph of the Important Notice rules out any representation that the information will be reviewed at any stage before the recipient acquires bonds. This is clear from the final sentence of that paragraph.
69 In my judgment, on the face of it, this relieves Goldman Sachs of any obligation to carry out any investigation of its own into the information provided in the SIM either at the stage SIM was issued or before an acquisition was made by a recipient of it.
70 Turning to the authorities, Mr Nash relied on four in support of his submissions: Smith v Land & House Property Corporation [1884] 28 Ch D 7; With v O'Flanagan [1936] Ch 575; Hummingbird Motors Ltd v Hobbs 1986 RTR 296; Sumitomo Bank v BBL [1997] 1 Lloyds Reps 487.
71... The facts in Sumitomo Bank are quite different and again I draw no assistance from it.
72 With v O'Flanagan is of some significance. It supports the proposition that when a representation has been made and the representor subsequently learns that it is not true he has a duty to correct the representation. Romer LJ said ...:

"The only principal invoked by the appellants in this case is as follows. If A with a view to inducing B to enter into a contract makes a representation as to a material fact, then if at a later date and before the contract is actually entered into, owing to a change of circumstances, the representation then made would to the knowledge of A be untrue and B subsequently enters into the contract in ignorance of that change of circumstances and relying upon that representation, A cannot hold B to the bargain. There is ample authority for that statement and, indeed, I doubt myself whether any authority is necessary, it being, it seems to me, so obviously consistent with the plainest principles of equity."

73 In the same case Lord Wright MR described that situation as one that might be described as fraud. He added..:

"… though nowadays, the Court is more reluctant to use the word "fraud" and would not

generally use the word "fraud" in that connection because the failure to disclose, though wrong and a breach of duty, may be due to inadvertence or a failure to realise that the duty rests upon the party who had made the representation not to leave the other party under an error when the representation has become falsified by change of circumstances."
74 My final conclusions on this issue are as follows. The only implied representation made by Goldman Sachs arising out of the SIM was as the judge found one of good faith. There was, in my judgment, no implied representation that the information provided in the Arthur Andersen reports annexed to the SIM was accurate. There was an express statement that Goldman Sachs would not review or check the information contained in the SIM. In my view, it follows that it is only if Goldman Sachs actually knew that it had in its possession information which made the information in the SIM misleading that it could be liable for breach of the representation of good faith, provided the necessary intention was proved. In effect this would amount to an allegation of dishonesty.
75 The judge held that the implied representation of good faith was a continuing representation. However, in my judgment, that must be seen in the context of the sentence in the SIM which states that Goldman Sachs will not review the information contained in the SIM. It seems to me that this underlines the necessity for IFE to plead and show dishonest conduct by Goldman Sachs before it can succeed on the implied representation found by the judge.
76 As to the information provided by the subsequent reports, the judge held that that information was not such as to make Goldman Sachs aware that the information in the Arthur Andersen reports annexed to the SIM was misleading. He distinguished between actual knowledge that the earlier reports were misleading and information which "… merely gave rise to a possibility that the information previously supplied was misleading". In my judgment, in the circumstances this distinction was justified. The former would give rise to an allegation of bad faith. The latter did not.
77 .... It seems to me ... that he did not find facts which demonstrated that the earlier Arthur Andersen reports were to the knowledge of Goldman Sachs misleading.... it seems clear that the judge found that it would have required some investigation of both sets of reports before it could be concluded that the information in the first reports was misleading. In my judgment, this is a finding which the judge was entitled to make.
78 In reaching this conclusion I am conscious that the handwritten note in the margin of the 19 May 2000 report and the e-mail of 21 May 2000, to which I have referred above, appear to indicate that Goldman Sachs had some doubts about the financial position of Finelist. I am also conscious of the fact that no evidence was called on behalf of Goldman Sachs. Nevertheless, in my judgment, the judge was entitled to reach the conclusion that it had not been demonstrated by IFE that Goldman Sachs had actual knowledge of information which caused the two reports annexed to the SIM to become misleading. In any event no allegation of bad faith has at any stage been made by IFE.
79 In summary, in my view the only route by which IFE could establish a duty on Goldman

Sachs to disclose the two reports of May 2000 to IFE is by way of a duty of care. As to that, for the reasons given by Waller LJ, with which I agree, that argument cannot succeed.

Can a minority bank force the majority to take particular action under the loan agreement?

In **New Bank of New England v The Toronto-Dominion Bank** 768 F. Supp. 1017 (SDNY 1991) the court found that the plain language of the loan agreement allowed the majority lenders to exercise a discretion to accelerate the loan, which also meant they had a discretion not to accelerate the loan:

... Under the express language of the applicable agreements NBNE cannot compel the majority lenders to accelerate and foreclose.
As NBNE itself alleges:
The Intercreditor Agreement provides that the agent may act in certain circumstances in accordance with the directions of the majority lenders, that is, the holders of more than 50% of the unpaid debt under the Agreement. The Senior Credit Agreement contains a similar provision. For example, the Senior Credit Agreement provides that a majority of the lenders may require the agent to accelerate the loan upon specified events of default. Defendants TD Bank, Provident and Prudential together constitute majority lenders under both the Senior Credit Agreement and the Intercreditor Agreement . . . .
Here, a majority of the Lenders have not directed or required acceleration or foreclosure. The discretionary language of the operative documents authorizes them to refrain from doing so.
In Carondelet Sav. & Loan Assn. v. Citizens Sav. & Loan Assn., 604 F.2d 464 (7th Cir. 1979), a bank that had purchased a participation in a loan alleged that the selling bank had improperly refused to foreclose upon the borrower's default. The court held that where the participation agreement "specifically granted the [selling bank] authority to determine when to foreclose," the selling bank "clearly had the authority not to foreclose." 604 F.2d at 469. While the form of the loan participation at issue in Carondelet differed from the syndication in this case, and while the selling bank in that case had express authority under the agreement to act on behalf of all the participating lenders, Carondelet, nevertheless, establishes that the discretionary power to declare a default must also include the power not to do so....

NBNE asserts that while the agreements may not have expressly given it the right to insist on foreclosure, the explicit terms of the Credit Agreement and the Intercreditor Agreement must be interpreted as implying such a right.

Courts have generally refused to rewrite agreements to provide minority lenders with any rights, such as the "implied" right sought here by NBNE, which are not expressly set forth in the agreements..... Nor is there any basis for reading fiduciary or other duties into agreements "among sophisticated lending institutions."...

Indeed, to the extent that NBNE's claim against the other Lenders is premised on a purported "implied" covenant between the Lenders, NBNE has expressly waived such a claim. Section 9(d) of the Intercreditor Agreement .. specifically provides that none of the Lenders shall have any liability to each other for any action or omission in connection with, among other things, the Credit Agreement or the Intercreditor Agreement, "except as expressly provided" in those agreements. There is no question that such a limitation of liability among parties such as the lenders here is enforceable under California law. ..

In an effort to avoid summary judgment, NBNE has argued that the agreements must be considered ambiguous because the interpretation advanced by the moving Lenders has effectively created a stalemate: while Noble's default has not been waived, it has also not been acted upon. NBNE asserts that this stalemate could not reasonably have been contemplated by the parties, and that this indicates that the Lenders' interpretation does not reflect the parties' intentions when the documents were signed. NBNE's proposed interpretation is that because the Credit Agreement requires NBNE's consent to a restructuring and because it will not agree to a restructuring but, instead, prefers to accelerate and foreclose, the majority lenders are required to agree to accelerate and foreclose.

However, the document specifically provides that upon Noble's default the vote of a majority of the Lenders is required in order to exercise the remedies of acceleration and foreclosure. There is no provision in the Senior Credit Agreement for a minority lender such as NBNE to compel such an acceleration and foreclosure, and indeed, no provision which even suggests such authority.

Where, as here, the meaning of an agreement among sophisticated parties is unambiguous on its face, the agreement does not become ambiguous simply because one of the parties later asserts that it intended a different interpretation...

Nor should the court read an ambiguity into an agreement merely because one of the parties becomes dissatisfied with its position under the plain terms of the agreement...

All of the circumstances indicate that the parties to these agreements were

sophisticated institutions, dealing with the central issues of their business. As such, there is no basis to presume that they intended a result other than that required by the language of their agreements -- stalemate or not.

In addition, NBNE's assertion that the Majority Lenders have an "implied obligation of good faith" to accelerate and foreclose is barred by § 9(d) of the Intercreditor Agreement and Section 12.1 of the Credit Agreement, which states with respect to TD Trust:

no implied covenants, functions, responsibilities, duties, obligations or liability shall be read into this Agreement or otherwise exist against the Funding Agent.

In each of the cases cited by NBNE in support of this claim of "good faith obligation," the party alleged to have breached the implied duty of good faith either wrongfully exercised some contractual power to its exclusive benefit or wrongfully denied the existence of a contractual obligation, again to its exclusive benefit. Here there is no allegation that the other Lenders have acted in a fashion intended to benefit themselves at NBNE's expense, but only that the two sides disagree on which course of action will produce a better recovery on the troubled loan.

Thus, NBNE has no "right" to accelerate, nor is there any "promise" to accelerate. Acceleration is a remedy that can only be provided by -- and exercised in accordance with -- contract... The agreement here does provide for the remedy, but only where it is approved by a majority of the Lenders.

Nevertheless, although acceleration and foreclosure are contractual remedies which may not be exercised without a majority vote of the Lenders, NBNE is free to pursue its own remedies at law by suing Noble to collect on its debt to NBNE. Section 13.3 of the Senior Credit Agreement provides in pertinent part:

The rights, remedies, power and privileges herein provided are cumulative and not exclusive of any rights, powers and privileges provided by law or in equity...

In summary, the language of the controlling agreements is unambiguous and no implied obligation can be constructed, impasse or no...

Adherence To The Terms Of The Agreements Does Not Constitute Negligence Or Wilful Misconduct

With respect to NBNE's third claim, for negligence or wilful misconduct, the defendants again rely upon § 9(d) of the Intercreditor Agreement, which provides that no creditor "shall have any liability . . . except as expressly provided herein." Although such an exculpatory provision is to be strictly construed under California law ...even a strict

construction of this language furnishes a defense to the Lender defendants here.
As for TD Trust, although Section 7(a) of the Intercreditor Agreement provides that the agent "shall be liable for its own gross negligence or wilful misconduct," the misconduct alleged is the failure of the Lenders other than NBNE to declare a default, rather than TD Trust's failure to act upon such a declaration. Since no duty is owed to NBNE to declare a default, the failure to make such a declaration does not constitute negligence.

In an English case, **Redwood Master Fund Ltd v TD Bank Europe Ltd** [2002] All ER (D) 141, Rimer J. refused to hold that the majority lenders' power to vary the terms of a syndicated loan agreement[39] was subject to an implied term that the power would be exercised bona fide for the benefit of the lenders as a whole because such an implied term did not reflect the intention of the parties, and such a restriction on the power to vary the agreement might be unworkable. Rather the court should assess whether the power was being exercised in good faith for the purpose for which it was conferred. I am including a very long excerpt from this decision because the facts are very complex. But note that this case is related to the issues in the Elliot cases we looked at earlier and the EMCA model clauses. Any time there may be conflicts between the interests of different groups and a majority has the power to decide outcomes these issues will arise (this is like the close corporation situation where a majority's power to take action may be limited by reference to ideas of good faith). Consider the excerpts from the judgment. **Do you agree with the judge about the appropriate approach to this issue?**

9. Clause 2.1 of the facility agreement provided for three separate facilities to be available to the borrowers: Facility A (hereafter, but not always, simply "A"), a revolving credit facility of Euro 750m; Facility B ("B"), a term facility of Euro 2.75 billion; and Facility C ("C"), a term facility of US$3475m and Euro 95m. Schedule 1, Part II, set out the proportions in which each lender assumed commitments under the three facilities. Fifteen of the 38 lenders assumed C commitments; and 26 lenders (including three who had assumed C commitments) assumed A and B commitments: no lender assumed an A or B commitment without also assuming the other. The amounts of the A and B commitments varied as between the lenders, but in each case the lender's B commitment was 3.66 times the amount of its A commitment, with each lender holding the same proportionate A commitment as it did a B commitment. That is of some

[39] The borrower in this case was United Pan-European Communications NV.

significance, because if the position had remained the same down to the time of the modified waiver letter, it is improbable that any complaint of the type raised in this action could have arisen. The complaint has arisen because, since the date of the facility agreement, the commitments have been the subject of dealings on the secondary debt market, so that the position by the time of the modified waiver letter was that not all lenders held similarly proportionate A and B commitments. By then, a minority in number and value of lenders (including the claimants) held only A commitments, or else held A commitments in proportions exceeding those of their B commitments....

The cross-default
22. UPCNV was due to pay interest on its bonds on 1 February 2002, although it had a period of grace (expiring on 3 March -2002).within which to pay. By January 2002, a question had arisen as to whether it would pay that interest. Its failure to do so would constitute a cross-default under the facility agreement for the purposes of clause 18. Subject only to any agreed waivers which might be agreed under clause 25, the effect of that would be, amongst other things, to absolve the lenders from any obligation to make further advances under the facility agreement. This was because the cross-default would be an "event of default" under the facility agreement for the purposes of the condition precedent imposed by clause 4.2(b). In addition, any such default would subject the borrowers to the risk of the acceleration provisions of clause 18.21.
23. The risk of a default in the payment of the interest due on the bonds - and the default itself when in due course (as it did) it happened - were therefore potentially serious, matters as regards the UPCD group, which was dependent, for its cash needs on the facility agreement. They were of course also potentially serious matters for UPCNV itself, and they led to negotiations between UPCNV and its bondholders with a view to UPCNV's capital restructuring. These negotiations occupied the succeeding months, until eventually on 30 September 2002 a formal agreement was concluded as to the way forward, although it was not one that finally resolved the matter. The achievement of the proposed restructuring was going to, and still does, require both Chapter 11 proceedings in the USA, and "Akkoord" proceedings in the Netherlands.. The action is concerned solely with the effect of UPCNV's cross-default on the UPCD facility agreement, and the steps taken since February 2002 by the majority lenders to grant UPCD a waiver of the consequences of the default. Those steps resulted in the granting of a series of short-term temporary waivers, expiring on 27 September, and ultimately in the modified waiver letter signed on that day, about which the claimants complain.

The original waiver letter
24. Recognising the problems which would arise in the event of a cross-default by UPCNV, towards the end of January 2002 Mr Okhuijsen (the treasurer of the UPC group, including UPCD) and Mr Evans (a managing director of the legal department of UPCNV) contacted Mr

Bingham and Mr McPherson of the TD Bank group, in particular in their capacity as spokesmen for TD Bel, the facility agent. They warned of the risk of a cross-default and asked TD Bel to take the lead in co-ordinating the banks' response to UPCD's request for a waiver of the default provisions should the need arise. On 1 February, Mr Okhuijsen told Mr M0herson that UPCNV would not be making the interest payments due on that day.
25. As a result of this, TD Bank and another lender, J P Morgan Chase ("JPMC"), decided that an ad hoc committee of lending banks would need to be established to conduct the waiver negotiations on behalf of the lenders generally. The first meeting . of the lenders took place on 6 February. TD Bel convened the meeting, by notice given only to those lenders entitled to receive non-public information about UPCD's finances. This circulation was so restricted because the meeting would be discussing such non-public information. I shall, for brevity, refer to this class of lenders as "non-public lenders." The reason that other lenders ("public lenders") were not entitled to the like information was because they traded in public securities, and for them to trade in UPC group stocks whilst in possession of non-public information could put them in breach of SEC regulations. This was not necessarily a bar to their receipt of such information, provided that they had first set up necessary Chinese walls or other mechanisms enabling them to receive it, but the onus was on them to notify TD Bel (as facility agent) they were so able. In fact, only a small percentage of lenders were public lenders. The only claimants who were parties (by novation) to the facility agreement at this stage were Goldentree MF and Goldentree Opportunities (the fourth and fifth claimants): the former held Euro 3 53m of B paper and the latter held Euro 1m of A paper. As they had not notified TD Bel that they were entitled to receive non-public information, they were not on the circulation list for the meeting.
26. I find that as early as this meeting the lenders expressed their wish that a term of any waiver to be granted to UPCD should be the overall reduction of the facility (it is the facility reduction that was ultimately achieved by the modified waiver letter which has given rise to all the trouble). The meeting approved the establishment of an ad hoc co-ordinating committee of lenders ("the CCL") comprising TD Bank, JPMC, The Royal Bank of Scotland Plc, Fortis Bank (Nederland) NV and Bank of America NA. The CCL's function was to negotiate with UPCD on behalf of those lenders supporting its role ("the consenting lenders'), which in fact represented an overwhelming majority in value of all lenders. The negotiations were conducted primarily by Mr Bingham and Mr McPherson (both of TD Bank) for the CCL and Mr Evans and Mr Okhuijsen for UPCD.
27. These negotiations led to the agreement of a temporary waiver on the terms of a letter from TD Bel to UPCD dated 1 March 2002 ("the original waiver letter). UPCNV had not in fact committed a cross-default by then (because the grace period was still running) but it did commit it on 3 March, when the period expired. The letter, therefore, strictly operated as an anticipatory waiver of the consequences of UPCNV's expected default. The waiver was for a limited period expiring on 3 June 2002 at the latest: subject to any further waivers, it would then be open to the lenders to exercise all their rights under the facility agreement.

28. The letter reflected the views of the consenting lenders. It referred to the establishment of the CCL. It imposed various conditions on UPCD. One was that by 1 March 2002 Euro 100m of outside money should have been injected into the UPCD group, by way of capital or subordinated loans, and Belmarken duly provided this cash. Another was that (subject to certain conditions) UPCD could draw a maximum of Euro 100m under Facility A (which was still wholly undrawn), for the purpose of applying such advances in the ordinary course of the business of the UPCD group. UPCD had to provide certain management information, business plans and budgets to the CCL, and Deloitte & Touche ("Deloittes") were to be appointed to review UPCD's business plans and forecasts on behalf of the CCL. The letter reflected that steps were being taken towards the restructuring of UPCNV's indebtedness.
29. On the same day, 1 March, the CCL issued a letter to lenders seeking their formal consent to CCL playing a continuing co-ordinating role, the letter envisaging (as happened) that TD Bank and JPMC would act as co-chairmen of the CCL. 94% in value of the lenders signed, up to the letter. Of the balance of lenders who did not. 3% had confirmed that they were only public lenders. The third to fifth claimants (HCM/Z, Goldentree MF and Goldentree Opportunities) subsequently signed up as well, and so received all non-public information circulated to lenders. Very much later, so did Redwood, the first claimant.

The claimants' acquisition of Facility A paper
30. The action is based on the claimants' complaint that the modified waiver letter later signed on 27 September 2002 discriminated against them as holders of A paper, and was manifestly unfair towards them. The heart of the complaint is that it entitled UPCD to draw on A solely for the purpose of prepaying part of the B drawings, at a time when (a) but for any waiver UPCD could not draw on A at all; (b) even with an unconditional waiver, the covenant restrictions prevented it from drawing sufficient A funds to make the prepayment; and (c) pending the completion of the restructuring of UPCNV (which was not expected to be achieved, if at all, before the end of March 2003), the solvency of UPCD was in doubt. The claimants make other complaints as well, to which I shall come, but I must first summarise the commitments the claimants acquired under the facility agreement, and when they did so.
31. Redwood bought Euro 14m of B paper on 8 February 2002, and Euro 7m of A on 9 April. It sold Euro 5m of B on 18 April and bought a further Euro, 5m of A on 3 July. At the date of the modified waiver letter, it held Euro 12m of A and Euro 9m of B. Gracie started acquiring and selling A and B paper on 10 May 2002. At the date of the modified waiver letter, it held Euro 7.5m of A and Euro 2m of B. HCM/Z bought Euro 5m of each of A and B paper on 16 April 2002, but sold the latter on 31 July. At the date of the modified waiver letter, it held Euro 5m of A, and no B. Goldentree MF purchased Euro 3.53m of B paper on 30 November 2001, and a further Euro, 1m on 15 February 2002. It sold all its B paper on 19 April. On 10 May, it started purchasing A paper. At the date of the modified waiver letter, it held Euro 22.12m of A, and no B. Goldentree Opportunities purchased Euro 1m of A paper on 30 November 2001, and bought

a further holding of Euro 2m on 15 February 2002. It sold the lot on 18 April, but then bought Euro, 4.6m of A on 30 August, which it also held at the date of the modified waiver letter. It had no B paper. Seneca started acquiring and selling A and B paper on 8 April 2002. At the date of the modified waiver letter, it held Euro 15m of A and Euro 4m of B.

32. Each claimant therefore held either only A paper, or else (as between A and B) predominantly A paper (meaning a greater percentage of A paper than of B paper). Each acquired the A paper it held at the date of the modified waiver letter with knowledge of UPCNV's cross-default and of the original waiver letter. At the time of each relevant (post cross-default) purchase, the A paper was trading on the secondary debt market at a discount of some 35%, and the claimants were paid a reverse premium reflecting that discount to take on their A commitments. Expressed generally, since the evidence does not disclose precise figures, for each Euro 100 they became committed to lend, they were paid about Euro 35.

The events leading to the signing of the modified waiver letter

33. A meeting of the consenting lenders took place on 16 May, at which UPCD and Deloittes made a presentation. Its purpose was to enable the lenders to learn about UPCD's projections for the future and determine the basis on which any extended waiver might be granted. HCM/Z was present (represented by Ivan Zinn), being the only non-public claimant at that stage.

34. The UPCD projections presented to the meeting showed that its total drawdown under the facility agreement would not exceed Euro 3.38 billion after 2002, and projected a drawdown of A in 2004 in order to make the first repayments then due under B and C. Various lenders made renewed requests for a reduction in the facility. Mr Bingham said in evidence that they included CIBC, and probably Goldman Sachs and Morgan Stanley. He said that support for such a reduction from others at the meeting was apparent.

35 I find that the lenders assumed that any such reduction would simply be in the undrawn facility. A was wholly undrawn, and Euro 70m of B was also undrawn, although B and C were otherwise fully drawn. Most lenders had interests in both A and B, and so a cancellation of the undrawn facilities would be in their interests. On 30 May, Mr McPherson of TD Bank circulated to the consenting lenders a list of the so-called "Asks" they had raised at the meeting. Items 1 and 15 referred respectively to "No further advances under the Facility Agreement" and "Facility reduction to reflect revised business model." The CCL's recorded response was that its assessment was that UPCD was unlikely to agree to a facility reduction.

36. On 31 May, the temporary waiver effected by the original waiver letter was further extended for a short period. I need not detail its terms, nor those of the subsequent further temporary waivers granted by TD Bel letters of 17 June, 1 July, 15 July, 29 July, 12 September and 23 September. The need for these renewed temporary extensions was to allow sufficient time for UPCNV to reach agreement with its bondholders as to the way forward to a capital restructuring of UPCNV.

37. On 11 June, TD Bank made a further note referring to the lenders' "Asks", including a

reference to the request for the facility size of "Euro 4 billion to be [reduced] to a lower amount given the revised business plan [which] shows a peak borrowing of Euro 3.4 billion." TD Bank's recorded comment in relation to that was that UPCD's management had previously stated that it planned to retain the facility at its then level, so as to provide it with long term flexibility. This note was circulated to the consenting lenders, including HCM/Z. On 13 June, Goldentree MF and Goldentree Opportunities joined with other lenders in confirming the role of the CCL and signed confidentiality letters with UPCD enabling them to receive non-public information.
38. On 23 July, UPCNV reached an agreement in principle with its external bondholders for a capital restructuring (UPCNV's major bondholder was UGC). A meeting of the consenting lenders (representing some 97% in value of the facility commitments) took place the following day. HCM/Z, Goldentree MF and Goldentree Opportunities were invited to it, but it is not clear whether they attended. UPCD, UPCNV and the advisers to the bondholders' steering committee were at the meeting. Those advisers outlined to the lenders the basis of the agreement that had been reached for the restructuring, and explained the method by which it was to be achieved and the timing of the steps to be taken to achieve it. The restructuring was to involve an exchange of debt for equity.
39. UPCD, UPCNV and the advisers then left, and Mr Bingham made a presentation to the lenders explaining why a further temporary waiver was required. He says a number of lenders again asked for a reduction, of the facility, and also for an upward negotiation of the commissions and margins payable under the facility agreement. Other lenders expressed concern as to whether UPCD could meet its financial covenants in and after the first quarter of 2003, and proposed that these should be revised so as to be in line with its business plan. The current waiver was due to expire on 29 July, and the lenders agreed a further 45-day extension so as to enable UPCNV to document its restructuring agreement with the bondholders. Mr Bingham assumed that any facility reduction would be in the undrawn A, and the inference is that the other lenders did as well.
40. On 8 August, Mr McPherson of TD Bank sent an informal list of the lenders' "Asks" to Mr Okhuijsen and Mr Evans of UPCD. Item 10 read "Facility Reduction/Pricing TBA". This led to a discussion on 9 August between Mr Okhuijsen and Mr Bracken of UPCD, and Mr Bingham and Mr M0herson of TD Bank. The former said that UPCD could not agree to any reduction in the facility, or to its repricing, and that the CCL would have to discuss these matters with UGC and UPCNV's bondholders.
41. This led to discussions over the following days between Mr Bingham. of TD Bank and Mr Fries of UGC, and to a meeting in Denver on 20 August between Mr Bingham, Mr Fries and Mr Schneider (also of UGC). Mr Bingham recorded the outcome in an e-mail he sent to Mr McPherson on 20 August. He wrote that "After we got past the threat of nuclear war" - suggesting the negotiations had not been easy - agreement was reached in principle that a continued waiver would be granted until the closing of the restructuring. Three conditions were to be imposed on UPCD immediately upon the grant of such waiver: (i) the payment to the

lenders of a waiver fee of 0.25 basis points, to be paid by a drawdown on the UPCD bank facilities (presumably A); (ii) an increase in the margin on all facilities by 150 basis points; and (iii) "Availability decreased by Eur 50OMM." This last was of course a reference to the agreed Euro 500m reduction in the facility (a Euro 4 billion one), which was in line with UPCD's projections showing a peak borrowing need of Euro 3.38 billion. Four further conditions were to be imposed on UPCD once the restructuring was closed. The only ones I need mention are those providing for a relaxation of the ratios by reference to which UPCD was able to draw on the facility, and the injection of Euro 125m cash into UPCD for equity. The evidence also includes an e-mail of 20 August from Mr Fries to Mr Okhuijsen and Mr Evans, setting out the terms of the agreement from UGC's perspective. He described four points as having been agreed, including "Availability: Reduced by 500 million (at time of waiver)", and three others as still under discussion.

42. I comment that in agreeing a Euro 500m reduction, Mr Bingham had to some extent departed from the consenting lenders' and the CCL's instructions. Both bodies had been aiming for a reduction of about Euro 400m, but Mr Bingham argued for a Euro 500m one, on the basis that he expected to be negotiated down. In the event, Euro 500m was achieved, and he did not suggest to UGC that a lower reduction would do. Mr Brisby made some point of this, but of course when the matter was put to the consenting lenders at their next meeting, on 4 September (to which I shall come), they knew the precise amount of the proposed reduction, and how it was to be effected, and raised no objection or concern about it.

43. Mr Bingham's evidence was that, although UGC had by now agreed a Euro 500m reduction in principle, it insisted that the details as to how it was to be effected, in particular its allocation between A, B and C, were to be decided by UPCD. Mr Bingham said that UPCD made it plain that it could not continue in business if the whole Euro 500m reduction was effected in A, and he realised by now that, contrary to his original assumption (and, I find, that of the lenders generally) UPCD would not agree to the reduction being effected simply by cancelling the undrawn facilities.

44. Following this, UPCD promptly devoted itself to working out how a Euro 500m facility reduction could be achieved consistently with its projected cash needs. Mr Okhuijsen asked his assistant, Mr Nooij, to prepare a financial model and he asked him to show the cancellation as all coming off B. Only Euro 70m of B was undrawn, so that any such cancellation would also require a minimum prepayment of Euro 430m of the B drawings, which could only be done by drawing on A. But the advantage to UPCD of achieving the reduction by this route was simple, namely that as the B repayments due in 2004 were a percentage of the outstandings as at 31 December 2003, it would assist UPCD's cash flow projections if those outstandings could first be reduced as much as possible. I find that UPCD took the view that it had a right under clauses 72 and 7.3 of the facility agreement to draw, cancel and prepay in this way, although it appears to me that such a view was strictly misplaced. This was because, at the time, UPCD was in default and was only enjoying a temporary waiver. The terms of any extended waiver

were dependent on agreement with the lenders, so that UPCD's rights under the facility agreement were more limited than it may have thought.
45. At the same time as UPCD was working on its own financial model, TD Bank was working out for itself how the facility reduction might be achieved. By 22 August, Mr McPherson had calculated that, in light of UPCD's figures for 2003 and 2004 (UPCD had not provided figures for any later years), the reduction would have to fall mainly on the drawn facilities (B and C) and not just on the undrawn A, and so would require some prepayments. At 1.37 pm on 22 August, he sent an e-mail to Mr Bingham. enclosing a model he had prepared, saying that it "shows all B but to make it work cash flow wise it will probably be Euro 100 A, Euro 350 B and Euro 50 C. (B & C don't make much difference but I think we need to offer something to get the C lenders onside)." His last comment reflected that the proposed reduction would necessarily involve prepayments of drawn facilities, and the 'lenders' support for the proposal might depend on their being given a share of it.
46. On the same day, 22 August, Mr Nooij told Mr Okhuijsen that his further thoughts revealed that UPCD's repayment profile would be substantially improved if the reduction were effected by cancelling Euro 83m of A and Euro, 417m of B. Mr Okhuijsen was satisfied that this was the optimal solution and he telephoned Mr McPherson that evening to tell him. Mr Nooij and Mr McPherson had, therefore, been independently thinking along similar lines. Mr Okhuijsen explained in evidence that the benefit of the proposed allocation was that it optimised the repayment profile under the facility agreement, and hence UPCD's ability to continue in business and ultimately to repay all lenders in full.
47. At some uncertain point TD Bank had raised with UPCD that part of any prepayment should also be allocated to the C lenders, but on 23 August, Mr Nooij advised Mr Okhuijsen that there was good reason for not prepaying and cancelling any of C, namely that it would result in higher repayments in 2004 and 2005 (the detailed reasons why do not matter). On the same day, Mr Okhuijsen sent TD Bank a revised model showing the proposed cancellation of A and B, and the prepayment of the latter. The model showed the drawdown on A that would be necessary in order to make the B prepayment. Mr Okhuijsen also spoke to Mr Bingham and Mr McPherson on the telephone, although according to Mr Okhuijsen their conversation did not concentrate on the allocation of the facility reduction, and he says that Mr Bingham and Mr McPherson expressed no concern about it. It focused rather on UPCD's short term liquidity needs, the banking covenants and its ability to carry out currency and interest hedging. This aspect of the discussion (relating in particular to the banking covenants) was directed to enabling UPCD -to draw down in 2002 the full Euro 100m provided for by the original waiver letter rather than just Euro 67m, which was the limit in practice permitted by the constraints of the covenants. Mr Bingham's evidence was that he agreed with Mr Okhuijsen that TD Bank would put Mr Nooij's model to the CCL for discussion and consideration. Mr Okhuijsen accepted in cross-examination that he explained during this conversation that nothing would be going to the C lenders.

48. On 27 August, Mr McPherson circulated to the CCL members his perception of the details of the terms of the proposed waiver. These included the waiver fee to lenders, the margin increase and a Euro 500m reduction. As to the last, Mr McPherson said that exact split was yet to be confirmed, but was:

"... likely to comprise Tranche A reduced by Euro 83.3MM (11.1%), Tranche B Euro 366.7 MM (13.3%) and Tranche C Euro 50 MM (11.3%). Please note any voluntary prepayment/cancellation does not have to be made on a pro-rata basis as the company has the option of prepaying/cancelling individual tranches (Clauses 7.2 & 73 of the Facility Agreement)."

49. Mr McPherson explained further that, in consideration of agreeing to this, the lenders would be asked to agree to a covenant relaxation so as to enable Euro 100m to be available to UPCD during 2002. He explained that UPCD was in the course of obtaining bondholder approval to the package, and that the CCL should contemplate distributing it to the lenders prior to the meeting fixed for the following week. It appears that, although UPCD was clear (and had already told TD Bank) that the optimal allocation of the Euro 500m reduction could not include the C lenders, TD Bank was of the continuing view that it might be necessary to throw them a bone in order to enlist their support.

50. On about 3 September, Mr Okhuijsen spoke to Mr McPherson on the telephone. He said that UPCD had decided that the split would be exclusively between A and B, with the cancellation of Euro 83.25m of A and Euro 416.75 of B, and the prepayment of Euro 346.75m of the latter (the balance of Euro 70m being undrawn). Mr Okhuijsen explained that UPCD would draw on A in order to make the prepayment of B. There is some uncertainty as to the precise timing of this conversation, which Mr Bingham suggests was only very shortly before the holding of the lenders' meeting which took place in London on 4 September.

51. Mr Bingham. says he explained to the lenders at the meeting UPCD's proposed allocation of the Euro 500m reduction, about which they raised no questions or objections. This was the first time it had been put to them that the overall facility reduction that they had wanted from the outset would be effected by prepaying part of B by drawing on A. Mr Brisby made the point that TD Bank should have gone back to the lenders during the last week of August and explained to them that a Euro 500m reduction could not be effected simply in the undrawn facilities, but would have in part to be allocated to the drawn part. But I do not see why the matter could not have waited the few additional days until this meeting. Mr Bingham says that, following this meeting, there was a conference call with the US consenting lenders, so that they could be party to the presentation which had been made at the meeting. Mr Zinn, on behalf of HCM/Z, participated in this call. Questions were asked about the allocation, and Mr Bingham responded that UPCD had the right under the facility agreement to allocate any cancellation or reduction amongst the three facilities as it thought fit. In saying so, he appears to have shared UPCD's view, although for like reasons I have already given I regard Mr Bingham's view as similarly misplaced.

52. On 5 September, Mr Haddad, on behalf of Goldentree MF and Goldentree Opportunities,

telephoned Mr McPherson of TD Bank. He said he was not happy with what he called "the split" - the allocation of the reduction between A and B - and complained that TD Bank may have acted improperly. He was complaining that B was receiving a disproportionate share of the overall reduction, although he did not assert that the facility should not be reduced at all, or that any such reduction should be deferred until the restructuring of UPCNV had been finalised. Mr McPherson replied that UPCD had decided on the split, not TD Bank. Both Goldentree funds held only A paper. The effect of the proposal was that they would be required to suffer draw downs for the sole purpose of prepaying B. So, of course, would the other A lenders, but as regards most of them, and having regard to the relative size of their B holdings, that would have either a cash positive or, at worst, a neutral effect. This proposal was ultimately incorporated into the modified waiver letter, despite the claimants' objections, and I shall explain later in more detail its effects on the various lenders. On the same day, Mr Jonathan Kolatch of Redwood telephoned Mr McPherson and made complaints about the waiver fees being too low and that the banks were "rolling over."

53. It was only. at this point in the course of the negotiations with the lenders that TD Bank realised for the first that some lenders, like the two Goldentree funds, were A lenders only. None of the CCL members held only, or predominantly, A paper. There is no evidence as to what any of the lenders knew as to the extent to which there were lenders holding only, or predominantly, A paper. Mr Bingham admitted in cross-examination that "in hindsight" it could be said that the prepayment of B, was not in the interest of such A lenders. He explained that this was only "in hindsight" because it was not until about 5 September that he learned that some lenders held only A. But the modified waiver letter was not signed until 27 September, and in the meantime specific consideration could, had the CCL chosen to do so, been given to the interests of this sub-class of A lenders. Even by 5 September, Mr M0herson does not appear to have appreciated the potential effect of the reduction on certain A lenders. On that day he sent an e-mail to Gregory Hurley of TD Securities, saying:

"...In effect the split over Tranche A & B is no different to a cancellation of Euro 500 MM undrawn commitment under A as this will be drawn to reduce B. The split between the two tranches was determined by the company to give them the optimal maturity/repayment profile that they could achieve given the reduction being made. As Tranche A & B were sold to the bank market on a pro-rata basis it makes no difference to the lenders which tranche is cancelled."

Had A and B still been so held, Mr Mcpherson's last remark would have been right. But they were not, and it was wrong.

54. On 6 September, TD Bel sent all the non-public lenders a letter setting out the terms of the proposed modified waiver letter, of which it enclosed a draft. This reflected the method of facility reduction that had been agreed with UPCD. The letter explained that the UPCNV restructuring negotiations were on course, and that it was expected that the final document would be signed by the proposed effective date of the waiver, namely 16 September. It asked for letters of

consent to the modified waiver letter to be returned by 12 September. Also on 6 September, TD Bel circularised a fax letter to all public lenders, setting out the essential terms of the proposed further waiver. The lenders so circulated included Redwood, Gracie, Goldentree MF and Seneca. The explanations in this letter were short. It referred to the fact that UPCD had requested an extension of the current waivers until the earlier of 31 March 2003 or the completion of UPCNV's restructuring process. It explained that the letter was including only public information, and was not including a draft of the proposed waiver document, although it said that its understanding was that the document would be submitted to the SEC in due course. It summarised some of the proposed changes to the facility agreement, namely (i) the payment of 'a waiver fee to each lender on the earlier of the completion of the restructuring or 1 April 2003, (ii) an increase in the margin as from 16 September 2002, and (iii) a Euro 500m reduction to the facility by reducing A by Euro 83.25m to one of Euro 666,750,000m; and by reducing B by Euro 416.75m to Euro 2,333,250,000, involving a repayment of Euro 346.75m. It did not explain that the prepayment would be funded by a draw down on A, although Mr Bingham, suggested, and I consider he was right, that the readers of this letter would have assumed this. The letter also pointed out that there were to be some changes in the financial covenants in the facility agreement. It similarly asked the lenders to signify their consent to the proposed waiver by 12 September.

55. By 11 September, it was clear that there was to be a further delay in the agreement of the UPCNV restructuring document. TD Bank circulated the lenders again, saying that there would be a further short temporary extension of the current waiver to 23 September.

56. On 12 September, Cadwalader, Wickersham & Taft ("Cadwalader'), the claimants' solicitors, entered the scene. They wrote to TD Bel as facility agent. They identified themselves as acting for a group of ten lenders, including the claimants. They were responding to TD Bel's letter of 6 September (written to the public lenders) inviting consents to the proposed modified waiver letter. They summarised the proposals. They said that TD Bel was faced with a conflict of interest. They said the proposals were not in the A lenders' interests, and complained that no-one had been appointed to represent their interests. They asked for an agent to be appointed as a matter of urgency. They said the proposal to use A advances to prepay B advances was not permitted by clause 3.1(a)(i) of the facility agreement. They said the proposals operated to extend the A commitments, a matter which was the subject of the entrenched provisions of clause 25.2 (a point Mr Brisby conceded was bad). They asked that the proposed waiver letter should be made public so that their clients could make informed judgments on it.

57. On the same day, 12 September, Mr Haddad (of Goldentree MF and Goldentree Opportunities, and who was also interested in four other funds holding A paper) wrote to Mr McPherson asking for representation on the CCL. His. request was considered by the CCL on 13 September. The CCL did not reply in writing to Mr Haddad, but Mr Hurley of TD Securities spoke to him on the telephone, when Mr Haddad requested the convening of a meeting of

lenders to consider the position of the A lenders. Mr Bingham considered this to be excessive and declined to take this step, but said he raised Mr Haddad's points with the CCL at its meeting on 13 September. The CCL's view was that it would be counter productive to open up Mr Haddad's points. Mr Bingham's elaboration of this in his evidence was that the CCL considered that it was for UPCD to decide how to allocate the reduction between the three facilities, and they also had in mind that any debate about the respective positions of the A and B lenders would be likely to provoke the C lenders into asking for a slice of the reduction. The overall view was that this would all lead to a delay in getting a deal with UPCD, which would not have helped anyone, and in particular would not have helped the negotiations between UPCNV and its bondholders about the restructuring. Mr Bingham's evidence was that the CCL considered that this could have jeopardised the restructuring. The CCL's conclusion was, in Mr Bingham's words, that "there was too much to lose and nothing to gain in reopening the issue as to how the reduction was to be allocated as between the tranches. UPCD had been very adamant throughout that they would only accept a reduction of the facility if they were allowed to allocate it as between the tranches." Nor was the CCL prepared to agree that Mr Haddad should have a representative on it.

58. On 13 September, Redwood opted to receive non-public information relating to UPCD.

59. Allen & Overy, TD Bel's solicitors, replied on 17 September to Cadwalader's letter. They denied that TD Bel had a conflict of interest. They denied that the proposals involved any breach of clause 3.1(a)(i) and said that anyway the majority lenders could consent to any necessary amendment of that provision. They denied that the proposals involved anything requiring the unanimous consent of the lenders. They said that TD Bel disagreed that the draft modified waiver letter should be made public.

60. On 19 September, TD Bank circulated to the non-public lenders a draft of the modified waiver letter in its nearly final form. On the same day, they also circulated the public lenders. They invited all lenders to consent to a short extension of the current waiver from 23 to 27 September, and to consent to the modified letter itself. They asked for the consents to be returned by 23 and 27 September respectively.

61. Cadwalader replied to Alien & Overy on 20 September. They pointed out that all their clients held A commitments exceeding their B commitments (if any) and that the proposed facility reduction and prepayment would have the effect of reducing the B exposure whilst increasing the A exposure. The wrote that:

"Outstandings under the Facility are currently trading at a substantial discount; any further Advances made by [Cadwalader's A clients] would represent an immediate loss of capital value, whilst the opportunity to take a substantial prepayment in circumstances where such monies would not ordinarily be payable represents a considerable windfall to the Facility B lenders."

They pointed out that the majority lenders' power to waive defaults did not permit them to exercise their powers in a way prejudicial to the minority, and they referred to the decision of the Court of Appeal in Greenhalgh v. Arderne Cinemas Ltd. and Others [1951] Ch 286, in

particular to what Sir Raymond Evershed MR said at page 291 (a passage to which I shall come). They stood by their points in their earlier letter and said that "Notwithstanding the purpose clause, our clients cannot against their wishes be taken from a position where their commitments cannot be drawn due to default, to a position where they can be required to make further Advances." They said their clients reserved all their rights in respect of the implementation of the restructuring (a reference to the proposed modified waiver letter, not to UPCNV's restructuring), "including the right to withhold and/or cancel the funding of the undrawn Commitments."

62. On 23 September, a further short extension of the waiver was granted until 27 September, so as to enable the UPCNV restructuring document to be finalised. Allen & Overy replied to Cadwalader's letter on 25 September. They devoted two pages to disagreeing with Cadwalader's assertions, but I find it unnecessary to detail the points they made. None could be said, on their face, to have irrefutably trumped all the cards Cadwalader had played.

63. By 27 September, the CCL had received the overwhelming consent of the majority lenders (81.76% in value) to the modified waiver letter, and on that day TD Bel circulated a copy of the final form of the letter, as signed, to lenders. The letter became effective on 30 September: paragraph 11 made it conditional on evidence that the UPCNV restructuring agreement had been signed by all parties, and it was then that the condition was satisfied. Also on 30 September, Cadwalader replied to Allen & Overy, saying they did not consider that the majority lenders had authority to give effective directions in relation to the waiver. On the same day, they copied to UPCD the correspondence they had written to Allen & Overy, and asserted that they considered the waiver to be ineffective.

The Modified Waiver Letter dated 27 September 2002

64. This is a letter from TD Bel to UPCD. It recites that its effect was to extend until 31 March 2003 the temporary waivers hitherto in place, and that the reason the majority lenders had agreed to it was to allow time for the completion of UPCNV's restructuring. As I have said, that was going to require both Chapter 11 proceedings in the USA and "Akkoord" proceedings for a compulsory composition in the Netherlands. In so far as the proceedings towards a restructuring might themselves constitute events of default under the facility agreement, they were to be waived until 31 March 2003, and would be permanently waived if the restructuring went through, when the slate would be wiped clean. Otherwise any such defaults would thereupon cease to be the subject of any waiver.

65. A principal purpose of the modified waiver letter was to reduce the level of the facility available under the A and B commitments. This was dealt with by paragraph 5, headed "Voluntary prepayment and reduction of Commitments". By paragraph 5.1, UPCD gave notice to TD Bel (as Facility Agent) of:

"...cancellation of a total of Euro 500,000,000 of the Total Facility A Commitments and the Total Facility B Commitments in the amounts set out in Schedule 1 and prepayment of the Facility B

Advances in the amount set out in Schedule 1 (being the amount necessary to ensure that the drawn amounts under Facility B do not exceed the Total Facility B Commitments following the above cancellation)."
66. Schedule 1 provided for the cancellation of Euro 83.25m of the A commitments, and Euro 416.75m of the B commitments, the total cancellation therefore being of Euro 500m. Schedule 1 further provided for the prepayment of Euro 346.75m of the B advances, such prepayment being necessary in order to ensure that the amounts then outstanding under B did not exceed the total B commitment as reduced.
67. The cancellation and prepayment were to take place on 7 October 2002. Paragraph 5.3, of the letter provided that:
"(a) For the avoidance of doubt, it is agreed that amounts may be drawn down under Facility A for the purposes of repaying all of the Facility B Advances referred to in Schedule I."
That was included to remove any doubt as to whether. but for it, UPCD would have been entitled under clause 3.1(a)(i) to draw on A in order to pay B.
68. Paragraph 6 of the letter provided for the payment of a waiver fee to TD Bel within five business days of the completion of the UPCNV restructuring, the fee to be distributed between all lenders pro rata to their then respective commitments. That was, therefore, in effect a conditional obligation, as was the provision in paragraph 8 requiring UPCD, within two business days of the completion of the restructuring, to procure the injection into UPCD of Euro 125m of cash, either for equity or by way of subordinated loans.
69. Schedule 2 to the letter made certain amendments to the terms of the original waiver letter. Schedule 3 imposed certain amendments to the facility agreement, including the deletion of clauses 4.3(a)(ii) and 4.3(b) of the facility agreement, which were necessary in order to vary the existing financial covenants so as to enable UPCD to draw down the A funds with which to make the B repayments (their current effect limited the available A drawings at that point to Euro 67m). Paragraphs 7 and 8 of Schedule 3 increased the margin. Paragraph 11 modified the provisions of clause 17 of the facility agreement so as to relax the conditions under which UPCD was entitled to call for a draw down under the facilities.

Subsequent events
70. On 2 October 2002, UPCD served notice of cancellation of Euro 83.25m of the A commitments and of Euro 416.75m of the B commitments, and on the same day it served notice of intended prepayment of Euro 346.75m of the B advances. In order to have the cash with which to do so, it served a request on the A lenders for an advance of Euro 346.75m on 7 October.
71. All A lenders honoured this request apart from the six claimants and three small funds who either are, or were, represented by Cadwalader but who are not claimants in this action. The shortfall arising from the claimants' default was Euro 283m. UPCD funded the shortfall from its other cash resources and by a short-term loan of Euro 14m from TD Bank. In order to repay TD

Bank, and to have enough for its other working capital needs, UPCD made a further A draw down request, for payment on 14 October. This was for Euro 25m, but again the same nine lenders refused to honour it. The shortfall arising from the claimants' further default was Euro 2.2m. On the other hand, on 21 October UPCD also made a draw down request on the A lenders of further funds for working capital purposes. The payment was due on 25 October. The claimants did honour this request, albeit late, by making the requested advances on 28 and 29 October. Since such drawdowns could only be made under the modified waiver letter, whose validity the claimants challenge, those payments reflect an inconsistent stance on their part, although they were apparently paid without prejudice to their overall position that the modified waiver letter does not bind them. I did not understand it to be suggested that the making of those payments served to put the claimants out of court in this action.

The effect of the modified waiver letter on the various lenders

72. The evidence includes a schedule recording the "funds flow" on 7 October, the date on which the A lenders were required to honour the request for Euro 346.75m in order to enable UPCD to prepay that sum to the B lenders. The schedule lists 46 lenders with A and/or B commitments. 31 lenders had both A and B commitments; seven had only A commitments; and eight had only B commitments. It also lists six lenders with C Euro commitments, one of which also had A and B commitments, and the other of which was only in B. Of the, 46 A and/or B lenders, 29 consented to the modified waiver letter, three indicated that they did not consent to it, and no response either way is recorded against the other 14 (which last class includes the claimants). The schedule records whether each lender was a net receiver or net payer of funds on 7 October, or whether the effect on it was neutral (that is, that it paid out and received identical amounts in its capacities as an A and B lender).

73. Of the 46 lenders, the effect on 18 was neutral. This was because they held their A and B commitments in the same proportions as originally issued under the facility letter: as I explained earlier, a lender with, say, a 5% A commitment would also have a 5% B commitment. Such a lender would therefore pay (as an A lender) and receive (as a B lender) the same percentage of the A levy necessary to enable the B lenders to be repaid. Although, therefore, a total of Euro 346.75m needed to be raised from A lenders to prepay the B lenders, the effect of many A/B lenders being in this neutral position was that the true extent to which the B lenders benefited by a transfer of risk to the A lenders was in the relatively small amount of Euro 68,656,810.15. Of the 18, 14 consented to the modified waiver letter, three voted against it and one abstained: the last four were Citibank NA, Deutsche Bank AG, Morgan Stanley Dean Witter Bank Limited and UBS AG. In an e-mail of 12 September to Mr McPherson, Gisle Bendiksen of Morgan Stanley had observed that the reduction did not treat lenders equally, also pointing out that certain lenders only had B commitments "and will have outstanding debt repaid without having to provide tranche A funding." Eight of the 46 lenders were in this class.

74. Of the remaining 28 lenders, 14 were net receivers and 14 were net payers. Eight of the net

receivers (including JPMC, a co-chairman of the CCL) held only B commitments, and the remaining six (including TD Bank) held proportionately greater B commitments than A commitments. Subject to a twist in the tale to which I shall come, TD Bank was the largest net receiver under the modified waiver letter, receiving Euro 24,979.184.80. The 14 net payers included seven lenders who held only A commitments, with the other seven holding predominantly A commitments.
75. The seven net payers who were only A lenders included Cisco Systems Finance International, which faced a net payment obligation of Euro 32,363,333.33, the largest net payment faced by any lender. Cisco consented to the modified waiver letter, a feature which. if unexplained, might be viewed as significantly unhelpful to the claimants' case. However, some late (apparently somewhat fortuitous) disclosure revealed that Cisco had a switch option entitling it to require TD Bank and Chase Manhattan Plc to take its A commitment off their hands and replace it with a B commitment, and with it the obligation to make the payment I have mentioned. Cisco exercised that option on 30 September, an action which would suggest that, despite its consent to the modified waiver letter, it did not regard the letter as favourable to itself as an A lender. The result is that TD Bank and Chase had to pick up that particular tab, so reducing TD's net receipts and converting Chase into a net payer. I think it probable that at least Mr Bingham had forgotten about Cisco's option. This group of seven lenders (those solely in A) also included Goldentree MF, Goldentree Opportunities, HZM/Z and three other funds. After Cisco, Goldentree MF faced the largest net payment, of Euro 10,457,980. None of these six lenders consented to the modified waiver letter.
76. The seven net payers who held predominantly A commitments included CIBC World Markets plc (who paid out Euro 3,152,272.73), Credit Suisse First Boston (Euro 1,996,439.37) Goldman Sachs Credit Partners (Euro 1,277,431.17), and K Capital Offshore Master Fund LP (Euro 551,197.20), all of whom consented to the modified waiver letter. The other three did not consent.
77. The overall position with regard to those holding either only A commitments, or else holding predominantly A commitments (but leaving Cisco out of account, since I regard it as a special case) is that a substantial majority in value of the A net payers did not consent to the modified waiver letter, although a minority (four in number) did consent to it.

The claimants' complaints
78. The modified waiver letter was entered into at a time when the capital restructuring of UPCNV was, as it still is, in a state of uncertainty. It was not known then, is not known now and will not be known for some time whether the restructuring will be achieved. If it is achieved, the waiver effected by the modified waiver letter will become permanent. If it is not, there will or may be a question mark over the future viability of the UPCNV group, including the UPCD sub-group. It was, common ground in the evidence that if the proposed restructuring of UPCNV is not achieved, that will carry with it the risk that UPCD group may fail and be unable to pay its

debts. To the question why, in these circumstances, did the CCL negotiate the prepayment - requiring a drawdown on A - before it could be seen whether the restructuring was going to succeed or failed, the essence of Mr Bingham's answer was that the lenders were pressing for it (together with their other "Asks'), and the CCL took the view that it should obtain it for them immediately.

79. The claimants assert that against that background of admitted risk about UPCD's longer term viability, the modified waiver letter was manifestly unfair to the A lenders as a class, or at any rate to that minority of lenders who, like the claimants, held only A commitments, or else held predominantly A commitments. Because of UPCNV's cross-default, the A lenders had been absolved from any obligation to advance any funds to UPCD. The claimants recognise that it was open to the majority lenders to waive the default, and so render the A lenders liable to honour their lending commitments; and the claimants had even been paid a premium to take these commitments on. But whilst it is, or may be, one thing for the terms of a waiver to require the A lenders to advance funds for the working capital purposes of the UPCD group, it is, so it is said, quite another to require them to advance funds to UPCD in its present distressed state for the purpose of prepaying the B loans in respect of which no repayments are due until 2004. The effect of this aspect of the modified waiver letter was pro tanto to transfer to the A lenders the exposure, and with it the risk, which had hitherto been faced by the B lenders. To the extent that the exchange of B liability for A liability was of either neutral or cash positive effect as regards any particular lender, the modified waiver letter imposed no adverse change on that lender. But as regards that sub-class of A lenders of which the claimants are part, and which became net payers under the modified waiver letter, it required them to take over from the B lenders a real and measurable exposure at a time when UPCD's future solvency was in question. Mr Brisby submits that there is no good reason why, even if it were otherwise appropriate to reduce the facility in the manner provided for by the modified waiver letter, such reduction could not have been made conditional on the successful completion of the restructuring (although that is not a point his clients made prior to the modified waiver letter). He also points out that UPCD itself was only prepared to agree to procure the injection of the further Euro 125m of outside money into UPCD when and if the restructuring was successfully completed. Why, therefore, should the A lenders be compelled to commit their funds to UPCD in advance of that contingency? Moreover, Mr Brisby submitted that the reduction imposed by the modified waiver letter was manifestly discriminatory towards the A lenders, because it was disproportionate: it reduced the A commitment by 11.07%, whereas the B commitment was reduced by 15.16%. Mr Bingham's response to that in his evidence in chief was that these reductions Mo not appear to unduly favour Facility B Lenders over Facility A Lenders," which appears to recognise that the reductions do favour the former, but only to a due extent. Mr Bingham. adds though, as is clear from the evidence, that the CCL left to UPCD the method by which the reduction was to be achieved. Even after the claimants started complaining about the split, Mr Bingham and the CCL effectively ignored the position of the minority A lenders,

apparently in part on the basis that their objections could not prevent the majority lenders having their way, but I have also set out his concern about reopening the matter at that point in the negotiations which I regard as the main reason for not doing so. In addition, Mr Brisby made the point in his reply that even if there had simply been an unconditional waiver, the covenants to which UPCD was currently subject prevented it from drawing down more than Euro 67m in 2002. He pointed out that the only basis on which it was enabled to draw down sufficient A funds to repay the B lenders was. by the cancellation (in pursuance of the majority lenders' amendment powers) in the modified waiver letter of the provisions of clauses 4.3(a)(ii) and (b) of the facility agreement. I do not, however, understand-that to have been a point made by the claimants or Cadwalader prior to the execution of the modified waiver letter.

80. These are the claimants' main points, although Mr Brisby also submits that there was an additional element of unfairness in the further risk to which the modified waiver letter exposed the A lenders, that is the risk of the further draw down of the Euro 100m for working capital, a risk which was increased by the relaxation of the covenants enabling it to be drawn; and. related to this, he points to the yet further risk to which they are exposed, namely that if the UPCNV restructuring is successfully completed, it will be open to UPCD to draw on A to the full extent of its reduced amount.

The issues

81. The claimants' main point of complaint, therefore, is that the modified waiver letter discriminated against the A lenders as a class by imposing discriminatory disproportionate overall reductions in A and B, and, at a time when the future viability of UPCD was in question, subjected the A lenders as a class - or at least that minority sub-class of A lenders of which the claimants form part - to an unfair exposure to risk solely for the purpose of removing an equivalent risk from the B lenders.

82. Mr Brisby submitted that the majority lenders were not entitled to do that. He invokes the principle summarised in the judgment of Viscount Haldane in British America Nickel Corporation, Limited, and Others v. M.J. O'Brien, Limited [1927] AC 369. Viscount Haldane said, at p. 371:

"To give a power to modify the terms on which debentures in a company are secured is not uncommon in practice. The business interests of the company may render such a power expedient, even in the interests of the class of debenture holders as a whole. The provision is usually made in the form of a power, conferred by the instrument constituting the debenture security, upon the majority of the class of holders. It often enables them to modify, by resolution properly passed, the security itself. The provision of such a power to the majority bears some analogy to such a power as that conferred by s.13 of the English Companies Act of 1908, which enables a majority of the shareholders by special resolution to alter the articles of association. There is, however, a restriction of such powers, when conferred on a majority of a special class in order to enable that majority to bind a minority. They must be exercised subject to a general

principle, which is applicable to all authorities conferred on majorities of classes enabling them to bind minorities; namely, that the power given must be exercised for the purpose of benefiting the class as a whole, and not merely individual members only. Subject to this, the power may be unrestricted."

83. That principle has found similar expression in many authorities, both before and after the British America case, and Mr Brisby relied in particular on its restatement in the decision of the Court of Appeal in Greenhalgh v. Arderne Cinemas, Ltd. and Others [1951] Ch. 286. Sir Raymond Evershed MR gave the leading judgment, with which Asquith and Jenkins L.J.J. agreed. The case concerned the validity of a resolution altering the articles of association of a company. The challenge to it was based on the proposition that the resolution was not passed bona fide and for the benefit of the company as a whole, which earlier authorities had established was the touchstone for its validity. After referring to certain of those authorities, including two decisions of the Court of Appeal, the Master of the Rolls said, at p. 291:

"Certain principles, I think, can be safely stated as emerging from those authorities. In the first place, I think it is now plain that 'bona fide for the benefit of the company as a whole' means not two things but one thing. It means that the shareholder must proceed upon what, in his honest opinion, is for the benefit of the company as a whole. The second thing is that the phrase, 'the company as a whole', does not (at any rate in such a case as the present) mean the company as a commercial entity, distinct from its corporators: it means the corporators as a general body. That is to say, the case may be taken on an individual hypothetical member and it may be asked whether what is proposed is, in the honest opinion of those who voted in its favour, for that person's benefit.

I think that the matter can, in practice, be more accurately and precisely stated by looking at the converse and by saying that a special resolution of this kind would be liable to be impeached if the effect of it were to discriminate between the majority shareholders and the minority shareholders, so as to give to the former an advantage of which the latter were deprived. When the cases are examined in which the resolution has been successfully attacked, it is on that ground."

84. Of course, that case concerned the articles of association of a company, so that the parties interested in the matter included not just the shareholders, but also the company as a separate entity. There is no equivalent of the company in the present case, but Mr Brisby submitted, and the point was not controversial, that the principles outlined by the Master of the Rolls are equally capable of applying to the manner in which a majority of a class of lenders conducts itself in relation to matters affecting the whole class, and this is shown by the British America case.

85. In reliance on what he says is the applicable principle, Mr Brisby advanced his case on two alternative grounds. He said, first, that this is a case in which the claimants could show what he called a subjective lack of good faith by the majority lenders. Alternatively, he said they could at least show that, viewing the matter objectively, no reasonable lender could have concluded that

the modified waiver letter was in the interests of lenders as a whole. He said that proof of either alternative way of putting the case was sufficient to entitle the claimants to succeed. Those alternative ways of putting a case such as the present do, I consider, find support in the authorities. This is illustrated, for example, by the Court of Appeal's decision in Shuttleworth v. Cox Brothers and Company (Maidenhead), Limited, and Others [1927] 2 KB 9, one of the decisions referred to in Greenhalgh. The case concerned the validity of the alteration of a company's articles, being one whose effect was to deprive the plaintiff of his position as a permanent director. The case was in part based on the claim that the majority was motivated by bad faith towards the plaintiff. Proof that the resolution had been promoted by reasons of vindictiveness or malice towards the plaintiff would, or at least might, have been sufficient to enable him to succeed, since it could be said that its object was to do him harm rather than the company good (see, in this context, the observations of Lord Sterndale MR in Sidebottom v. Kershaw, Leese and Company, Limited [1920] 1 Ch. 154, at 161). The judge, however, ruled against the allegations of bad faith, and the Court of Appeal upheld that finding. But the possibility of a successful challenge to the resolution viewed simply on an objective basis still remained. Bankes LJ identified, at p.18, the relevant test as being whether the alteration of the articles was in the opinion of the shareholders for the benefit of the company. He said:
"By what criterion is the Court to ascertain the opinion of the shareholders upon this question? The alteration may be so oppressive as to cast suspicion on the honesty of the persons responsible for it, or so extravagant that no reasonable men could really consider it for the benefit of the company. In such cases the Court is, I think, entitled to treat the conduct of shareholders as it does the verdict of a jury, and to say that the alteration of a company's articles shall not stand if it is such that no reasonable men could consider it for the benefit of the company. Or, if the facts should raise the question, the Court may be able to apply another test - namely, whether or not the action of the shareholders is capable of being considered for the benefit of the company."
86. Scrutton LJ made observations to much the same effect. He said, at p. 23:
"Now when persons, honestly endeavouring to decide what will be for the benefit of the company and to act accordingly, decide upon a particular course, then, provided there are grounds on which reasonable men could come to the same decision, it does not matter whether the Court would or would not come to the same decision or a different decision. It is not the business of the Court to manage the affairs of the company. That is for the shareholders and directors. The absence of any reasonable ground for deciding that a certain course of action is conducive to the benefit of the company may be a ground for finding lack of good faith or for finding that the shareholders, with the best motives, have not considered the matters which they ought to have considered. On either of these findings their decision might be set aside."
87. I say straight away that I am unable to accept the claimants' case in so far as it based on what Mr Brisby referred to as subjective lack of good faith. That is simply a politely phrased allegation. of subjective bad faith, and appears to amount to an allegation that the majority

lenders in general, and TD Bank in particular, were motivated in promoting the modified waiver letter either by (i) a wish to improve their own position at the expense of the A lenders, or (although I do not in fact understand the claimants to have suggested this) (ii) by motives of vindictiveness or malice towards the claimants and other A lenders in the like interest. There is no evidence from any of the majority lenders other than TD Bank, and I feel quite unable to conclude that any of those other lenders was motivated in its decision to consent to the modified waiver letter by any sort of considerations of bad faith towards anyone. It is not even clear to what extent any of them (apart from those on the CCL, and those who were themselves destined to be net payers) were aware that there were sub-classes of A lenders who would be net payers ' as a result of the modified waiver letter. Nor am I prepared to make any findings of bad faith against TD Bank or any other lender on the CCL. It is true that they were informed of the essence of the claimants' concerns in September, and made a decision not to raise the points with the lenders. But in doing so, I find that they were not motivated by considerations of self-interest at the expense of the A lenders, or by any injurious ill-will towards the claimants. They were instead concerned that to do so at that stage in the operation might derail the restructuring negotiations, and they anyway did not consider that the minority's objections could make any difference to the outcome of the waiver negotiations. They may or may not have been misguided in that approach, which is something I will have to consider. But I have no hesitation in concluding that it was in no manner influenced by anything that might fairly be characterised as bad faith. In my view, if the claimants are entitled to succeed in this action, it can only be on the basis that, viewed objectively, the modified waiver letter was sufficiently discriminatory and unfair towards that sub-class of A lenders to which the claimants belong to justify the finding that the letter was not for the benefit of the lenders as a whole, or cannot be regarded as being capable of being considered to be for their benefit, or was otherwise an improper exercise of the clause 25 power.

88. Assuming that Mr Brisby is correct in his general submission as to the actions of the majority lenders, that will not, however, be enough to get the claimants home. They also have to show that UPCD is similarly affected by their challenge to the modified waiver letter, since on the face of it UPCD is able to say that it has concluded a binding contractual variation with TD Bel, and that it is nothing to the point that the claimants may have complaints about the manner in which TD Bel was given its authority to sign the letter. Mr Brisby's answer is that, prior to the signing of the modified waiver letter, UPCD had been copied in on all the correspondence that Cadwalader wrote to Allen & Overy and was expressly on notice that the claimants challenged TD Bel's authority to sign the modified waiver letter, and of course UPCD knew the terms of the modified waiver letter. On the facts, there is no dispute about that. If, therefore, the claimants can show that TD Bel had no authority to sign, UPCD signed up to the letter in the knowledge of that risk. In those circumstances, Mr Brisby submits that, if the claimants make good their case against the majority lenders, they must succeed against UPCD as well.

89. But is Mr Brisby correct that the Greenhalgh principle (as I shall call it) applies to this case?

If the claimants satisfy the court that the terms of the modified waiver letter were not for the benefit of all the lenders - because they were, on the face of it, ostensibly discriminatorily disadvantageous to a small sub-class of A lenders - is that enough to entitle the claimants to succeed?

90., If I may say so, Mr Brisby conducted his clients' case with very considerable skill, and advanced an excellent argument to me. But the excellence of his argument was matched by the excellence of those I also heard from Miss Jones and Mr Onions. I confess to having found this a difficult case. But, essentially for the reasons advanced by Miss Jones and Mr Onions, I have come to the conclusion that the principle by reference to which Mr Brisby asks me to decide the case is not the correct one.

91. The starting point is that the facility agreement is a commercial contract between a large multitude of lending bankers and their borrowers. It governs not just the lenders' relationship with the borrowers, but also the relationship between the lenders themselves. The contract has been carefully and professionally drawn and clause 25 devotes itself to setting out the contractual basis on which its. terms may be varied as between the lenders and borrowers. Save for the various entrenched provisions, which require unanimous consent before they can be altered, the lenders have, by their contract, empowered a two-thirds majority in value to consent to changes in the facility agreement, being changes which are capable of affecting and binding all of them. Clause 25 also empowered the majority lenders to agree to waivers under the agreement. The modified waiver letter is the fruit of the exercise of those powers.

92. The claimants' case is that that power is subject to the general principle of law relating to the manner in which a majority can bind a minority, namely that the power must be exercised bona fide for the benefit of the lenders as a whole. If so, it can only be on the basis that a principle to that effect is an implied term of the facility agreement. On ordinary principles, terms will only be implied into contracts if, as a matter of necessity, they are required for business efficacy purposes (The Moorcock (1889) 14 P.D. 64), or if it is a matter of obvious inference that they were intended to apply to the contract (Shirlaw v. Southern Foundries (1926) Ltd. [1939] 2 KB 206, per MacKinnon LJ at 227), or if they are necessary to give effect to the reasonable expectations of the parties (Equitable Life Assurance Society v. Hyman [2002] 1 AC 408, per Lord Steyn at 458). In the present case, if the suggested term is to be regarded as implied into the facility agreement, it would appear to me that it could only be on either the second or third basis.

93. It was Miss Jones who bore the main burden of dealing with this aspect of the defendants' arguments. It is of course no part of her case that clause 25 can or should be regarded as conferring on the majority an unfettered power to act arbitrarily, capriciously or oppressively, and she fully accepts that the power is impliedly subject to certain restrictions in the manner of its exercise. But her main point is that to treat clause 25 as being subject to an implied term that the power to waive and amend can only be validly exercised in a manner which can be seen to be for the benefit of the lenders as a whole - at any rate if that phrase is interpreted as carrying

the sense of the literal meaning of its language - would be likely, in readily foreseeable circumstances, wholly to paralyse the exercise of the power. Miss Jones submits that this cannot have been the intention of the parties to the facility agreement, and submits that no term having the potential to cause such an effect can be implied into it.
94. The reason for that is because the lenders under the facility agreement cannot simply be regarded as one unified class of lenders, all with a like interest. They are split into three classes, A, B and C, and the rights and interests of each class are peculiar to that class. I have set out how the different commitments were taken up by the original lenders when the facility agreement was entered into. But of course the agreement itself provided for those interests to change hands, and it was foreseeable at the time of the agreement that, as has happened, the original pattern of holdings would change. Miss Jones points out that it was similarly foreseeable at the time of the signing of the facility agreement that circumstances could arise in the future in which the commercial interests of one class might differ from those of another class. In such a situation, it would or could be almost inevitable that any decision by the majority in value of the lenders would or could be viewed as favouring one class over another. Put another way, it would or could in practice often be impossible for the majority to exercise their clause 25 powers in a manner which, viewed objectively, could be said to be for the benefit of each hypothetical member of each class.
95. The circumstances giving rise to the present action provide a good working example of the type of problems that could always be foreseen as capable of arising, but I consider that the point can be better illustrated by changing the facts a little. Assume that by February 2002 (i) the A commitments had been so dealt with on the secondary market that most of them were held by lenders with no B or C commitments, (ii) that the A commitments were wholly undrawn and the B and C commitments were fully drawn, and (iii) that UPCD then committed a default. At that point, it is quite likely that there would or might be a stark divergence of interest between the A lenders on the one hand and the B and C lenders on the other. The latter may conclude that the state of the economy is such that to realise their security at that point will result in enormous losses, and that the best prospect of being able to recover all or most of their debt will be to take a long term view, in the hope that the company can trade through its difficulties. For this purpose, they will wish to waive the default and enable the company to draw on the A lenders for the cash it will need to continue trading. But for the A lenders, who on my assumed facts comprise a class of lenders most of whom have no other lending commitments under the facility agreement, the picture is rather different. They have advanced no money to the company; the default has excused them from making any advances; and it is probable that they would prefer that there should be no waiver at all, so that they could instead advance their money to another institution more creditworthy than a company in the state of distress into which the borrower company had fallen. The situation would thus be one in which it could well be said that it would be for the positive benefit of the B and C lenders for there to be a waiver, but that a waiver would be to the positive detriment of the A lenders. If the claimants' argument

in this case is right, then it would not be open to the majority lenders to waive the default, since the A lenders could say that it would not be for the benefit of the lenders as a whole. So, in practice, the A lenders could veto it. They could paralyse the powers of the majority lenders at the just the type of crisis point in the lending transaction at which it might be thought that the facility agreement intended the majority lenders to be able to act.
96. I did not understand Mr Brisby to dispute that it was inherent in the scheme of the facility agreement that conflicts of this or a like sort could arise in the respective interests of the three classes of lenders. As I understood it, however, his position is that that possibility had and. has no relevant impact on his proposition that the Greenhalgh principle is impliedly incorporated into provisions of clause 25 of the agreement. His submission was that, if it should prove impossible for the majority to be able to exercise their powers in a non-discriminatory way, then the exercise of their powers would or might be paralysed, and that the only way forward would or might be to attempt to achieve the unanimous consent of the lenders to whatever was being proposed (which, ex hypothesi, is likely to be a vain attempt), or else to seek to achieve a scheme of arrangement between the borrowers and the lenders. In short, his point is that the clause 25.1 powers are only exercisable if they can be exercised in a manner consistent with the Greenhalgh principle. If they cannot, then they cannot be exercised at all.
97. I feel unable to accept that proposition quite in the terms in which it was put, which would appear to me to attribute to the parties to the facility agreement some improbable intentions. The main, although not the only, function of clause 25 is to establish a mechanism for dealing with problems of the varying types which might arise in the course of a facility agreement destined to have a nine-year life. When there are three different classes of lenders, the likelihood of differences arising between their respective interests is considerable. I have equally no doubt that it was the intention of the parties to the facility agreement that the requisite majority of the lenders - being a two thirds majority of all lenders, there being no provision for separate class meetings - should have the capacity to make decisions binding on all lenders. Moreover, often those decisions would have to be made in fairly short order, and it will be noted that clause 25 contains no machinery for consultation, discussion, representations or voting, although in practice (as happened in the present case) some sort of de facto mechanism would have to be set up by the lenders so that they could ascertain what the majority's views are. Mr Brisby's proposition that clause 25 is subject to an implied proviso which can operate to switch off its mechanism at the very time when it is probably most needed to be engaged is one I do not regard as well founded.
98. Having regard to the particular terms of the facility agreement, my view so far is therefore that clause 25 was and is intended to enable the majority lenders to make decisions binding on all three classes, even though it might perhaps be capable of being said by one class that the decision could not be said to be for its benefit. In the example I have earlier given, I can in particular see no reason why (if the facts showed it was a proper and responsible decision) the majority lenders should not agree to waive the default so as to enable the company to trade on

and, in doing so, to draw on the A facility. Nor can I see any good reason why, in principle, the majority lenders should not be able to agree that the financial covenants should be relaxed if that were necessary to enable the borrowers to draw down sufficient of the A funds as they needed for the purposes of their continued trading. The A lenders might well regard that as either actually, or potentially, prejudicial to them, and might, were the choice left to them, want no part of it; whereas the B and C lenders would regard it as the most beneficial way forward as far their own interests were concerned. But, in principle (and it will always depend on the facts), I can see nothing necessarily unfair towards the A lenders in a decision that the default should be waived and the covenants relaxed. The point is that the facility agreement is one under which all three lending classes are part of the long term lending package, and no class is entitled to say that it has had enough and wants to call a halt to its commitments. By signing up at the outset, each lender submits to the decision of the majority lenders at important forks in the road. The decision of the majority to allow the company to trade would, in my view, be exactly the type ' of decision that clause 25 was directed at enabling the majority lenders to make.

99. I was referred to a number of authorities on majority control, although none was of direct assistance for the purposes of the resolution of the present case. Most concern cases in which the persons affected by the relevant resolution were members of a single class, all with (in theory) like interests. The present case is different, because of the existence of the three classes with potentially differing interests. One authority which I did regard as of assistance in casting light on the correct approach to this case is the decision of the High Court of Australia in Peters' American Delicacy Company Limited v. Heath and Others (1938-39) 61 CLR 457. The problem there arose out of the company's somewhat ill-drawn articles of association. Articles 108 to 111 provided for cash dividends to be paid to members in proportion to the capital paid up on their respective shares. Article 120 provided that "Notwithstanding anything in any other article contained" profits could, with the authority of the company in general meeting, be distributed in the form of fully or partly paid shares in proportion to the number of shares held by the respective members. What gave rise to the dispute was a special resolution altering article 120 so that, on a capitalisation of profits, the distribution should be in accordance with the amount paid up on the respective shares of the members participating. The resolution was passed, but those with partly paid shares complained that it was unfairly favourable to the holders of fully paid shares. They complained that the resolution was not for the benefit of the company (meaning the corporators) as a whole, because they were prejudiced by it.

100. Nicholas J, sitting in the Supreme Court of New South Wales, upheld the complaints. The judgments of the High Court reversing his decision occupy some 40 pages, and were given by Latham CJ, Rich J and Dixon J, with McTiernan J agreeing. They include a careful examination of the English authorities touching on the "benefit of the company as a whole" point and provide an illuminating insight into the principles.

101. The value of the decision is that it arose out of a background in which the existing articles

gave rise to a conflict of interest between different groups of shareholders, and the purpose of the alteration was to resolve that conflict. Inevitably, the alteration could not please everyone, and the challenged resolution could not be defended on the basis that it could be said to have been for the benefit of the company - or the corporators - as a whole. There was, however, no suggestion of fraud or bad faith by anyone, and nor was there any evidence that the alteration was made with the object of oppressing a minority or depriving it of its rights (see the judgment of Rich J, at 490). At p. 495, after referring to various English authorities (including the Sidebottom and Shuttleworth cases, which I also referred to earlier), Rich J said:

"Where the very problem which arises contains as inherent in itself all the elements of a conflict of interests between classes of shareholders these authorities do not mean that the power of alteration is paralysed, they mean only that the purpose of bringing forward the resolution must not be simply the enrichment of the majority at the expense of the majority. The resolution in the present case was brought forward to solve a difficulty and make possible a capitalization. It can hardly be supposed that, the only solution of such a difficulty which can be lawfully adopted is that which gives the minority an advantage at the expense of the majority. In my opinion the case presents nothing but an ordinary example of an honest attempt on the part of the directors to clear up a difficulty by securing an alteration of the articles not unjust to any class of shareholders, but at the same time conserving the interests of the shareholders who form the great majority of the company."

102. I regard Dixon J's judgment as a particularly valuable one. He observed, at p. 503, that 'It, is one thing, however, to say that [the power to alter articles] is not unlimited or uncontrolled and another to define the grounds upon which an ostensible exercise of the power should be considered invalid." He then devoted considerable care to extracting from the authorities how those latter grounds can best be identified, observing en route, at p. 507, that:

"whatever may constitute bad faith, it is evident that, if a resolution is regularly passed with a single aim of advancing the interests of a company considered as a corporate whole, it must fall within the scope of the statutory power to alter articles and could never be condemned as mala fides. A positive test was therefore available, conformity with which necessarily spelt validity."

103. He then referred to the decision of the Court of Appeal in Allen v. Gold Reefs of West Africa Ltd. [1900] 1 Ch 656, and identified it as the source of the view, which can be found reflected in later authorities, that the validity or invalidity of the exercise of the power depended absolutely on whether that positive test had been satisfied, namely whether "the power had been exercised bona fide for the benefit of the company as a whole" and that nothing less would do. Dixon J appears to have regarded that as involving a wrong turn or emphasis. He referred to certain later decisions, including Brown v. British Abrasive Steel Co. Ltd. [1919] 1 Ch. 290, the Sidebottom case, Dafen Tinplate Co. Ltd. v. Llanelly Steel Co. (1907) Ltd. [1920]2 Ch. 124, and the Shuttleworth case. He then said this, at pp.511 to 513:

"If no restraint were laid upon the power of altering articles of association, it would be possible for a shareholder controlling the necessary voting power so to mould the regulations of a

company that its operations would be conducted or its property used so that he would profit either in some other capacity than that of a member of the company or, if as a member, in a special and peculiar way inconsistent with conceptions of honesty so widely held of professed that departure from them is described, without further analysis, as fraud. For example, it I would be possible to adopt articles requiring that the company should supply him with goods below cost or pay him ninety-nine per cent of its profits for some real or imaginary services or submit to his own determination the question whether he was liable to account to the company for secret profits as a director.

The chief reason for denying an unlimited effect to widely expressed powers such as that of altering a company's articles is the fear or knowledge that an apparently regular exercise of the power may in truth be but a means of securing some personal or particular gain, whether pecuniary or otherwise, which does not fairly arise out of the subjects dealt with by the power and is outside and even inconsistent with the contemplated objects of the power. It is to exclude the purpose of securing such ulterior special and particular advantages that Lord Lindley [in the Allen case] used the phrase 'bona fide for the benefit of the company as a whole.' The reference to 'benefit as a whole' is but a very general expression negativing purposes foreign to the company's operations, affairs and organizations. But unfortunately, as appears from the foregoing discussion, the use of the phrase has tended to cause misapprehension. If the challenged alteration relates to an article which does or may affect an individual, as, for instance, a director appointed for life or a shareholder whom it is desired to expropriate, or to an article affecting the mutual rights and liabilities inter se of shareholders or different classes or descriptions of shareholders, the very subject matter involves a conflict of interests and advantages. To say that the shareholders forming the majority must consider the advantage of the company as a whole in relation to such a question seems inappropriate, if not meaningless, and at all events starts an impossible inquiry. The 'company as a whole' is a corporate entity consisting of all the shareholders. If the proposal put forward is for a revision of any of the articles regulating the rights inter se of shareholders or classes of shareholders, the primary question must be how conflicting interests are to be adjusted, and the adjustment is left by law to the determination of those whose interests conflict, subject, however, to the condition that the existing provision can be altered only by a three-fourths majority. Whether the matter be voting rights, the basis of distributing profits, the basis of dividing surplus assets on a winding up, preferential rights in relation to profits or to surplus assets, or any other question affecting mutual interests, it is apparent that though the subject matter is among the most conspicuous of those governed by articles and therefore of those to which the statutory power is directed, yet it involves little if anything more than the redetermination of the rights and interests of those to whom the power is committed. No-one supposes that in voting each shareholder is to assume an inhuman altruism and consider only the intangible notion of the benefit of the vague abstraction called by Lord Robertson in Baily's Case [1906] AC 35, at p.39, 'the company as an institution.' An investigation of the thoughts and motives of each shareholder voting with the

majority would be an impossible proceeding. When the purpose of a resolution is spoken of, a phrase is used which refers rather to some characteristic implicit in the resolution in virtue of the circumstance or of some larger transaction of which it formed a part or step. It is not far removed from what Lord Sumner called 'one of those so-called intentions which the law imputes ... the legal construction put on something done in fact' (Inland Revenue Commissioners v. Blott [1921] 2 AC 171, at p. 218). But, when the very question to be determined is a conflict of interests, unless the subject matter is held outside the power, the purpose of the resolution, as distinguished from the motives of the individuals, often must be to resolve the conflict in favour of one and against the other interest.

In my opinion it was within the scope and purpose of the power of alteration for a three-fourths majority to decide the basis of distributing shares issued for the purpose of capitalizing accumulated profits or profits arising from the sale of goodwill, and in voting for the resolution shareholders were not bound to disregard their own interests. ... the resolution involved no oppression, no appropriation of an unjust or reprehensible nature and did not imply any purpose outside the scope of the power." (My emphasis in the second paragraph)

104. I regard Dixon J's judgment as a helpful guide as to how I should assess the attack levelled at the modified waiver letter by the claimants, and his emphasised observations were later echoed in Howard Smith Ltd. v. Ampol Petroleum Ltd. and Others [1974] AC 821, in which Lord Wilberforce said, at 835, after referring to the phrases "bona fide in the interest of the company as a whole" and "for some corporate purpose" that:

"Such phrases, if they do anything more than restate the general principle applicable to fiduciary powers, at best serve, negatively, to exclude from the area of validity cases where the directors are acting sectionally, or partially, ie improperly favouring one section of the shareholders against another. Of such cases it has been said:

"The question which arises is sometimes not a question of the interest of the company at all, but a question of what is fair as between different classes of shareholders. Where such a case arises some other test than that of the 'interests of the company' must be applied, ..."(Mills v. Mills, 60 CLR 150,164, per Latham CJ)."

105. I derive from these two authorities that, at least in a case such as the present, where there is a clear potential for conflicting interests between the three classes of lenders, an assessment of the validity of a majority decision exclusively by reference to whether or not it is "for the benefit of the lenders as a whole" is, at any rate if those words are applied according to their literal meaning, a misplaced one. The vice against which control on the exercise of majority power is directed is the potential for a dishonest abuse of that power. The starting point in assessing the validity of its exercise in any case must be to assess, by reference to all available evidence, whether the power is being exercised in good faith for the purpose for which it was conferred. If it is, then the mere fact that it can be shown that a minority of those affected by it have been relatively disadvantaged by it as compared with the majority cannot automatically mean it has been exercised improperly. Of course, if it can be shown that the power has been

exercised for the purpose of conferring special collateral benefits on the majority, or if the obtaining of such collateral benefits can be shown to have been the motive for the exercise of the power, that will be likely to lead to a conclusion that the exercise has been bad. It would not have been exercised for the purpose for which it was conferred, and its exercise in those circumstances would or might amount to a fraud on the minority. Equally, if the exercise of the power can be shown to have been motivated by a malicious wish to damage or oppress the interests of the minority adversely affected by it, then that too will vitiate the exercise, since that too will clearly amount to the commission of fraud on the minority, which is also obviously outside the scope and purpose of the power. Proof of matters of this sort may of course be difficult, and in many cases the complainants may have no independent evidence enabling them to level attacks on the exercise of the power on grounds such as these. They may, and usually will, be able to do no more than point to the manner of the exercise of the power and invite the inference that it is so manifestly disadvantageous, discriminatory or oppressive towards them that the only conclusion that can be drawn is that it must have been motivated by dishonest considerations inconsistent with a proper exercise of the power for the purpose for which it was intended. If the facts are strong enough, the court may well be prepared to draw such a conclusion.
106. I therefore reject any suggestion that, to succeed in this case, the claimants need only to show that the modified waiver letter can be said ostensibly to have discriminated against them and cannot, therefore, be said to be for the benefit of the lenders as a whole. I should, however, record that Mr Onions submitted that, on the facts, the package it contained both could and should be regarded as being of benefit to all lenders - or at least as being capable of being considered as being of such a benefit (see the citation in paragraph 85 above from Bankes Us judgment in the Shuttleworth case for the explanation of the latter submission). He emphasised that the package included identifiable benefits for all classes of lenders. The reduction of the overall facility (in which the A lenders share: the reduction they enjoy is in fact of the same order that they were due to enjoy in 2005, but it has now been accelerated by three years) was a positive benefit to all lenders, resulting in the lenders enjoying proportionately increased security for an overall reduced liability. In addition, waiver fees are to be paid and the interest rates were increased. The claimants share in all these things, and Mr Onions said that all they are really complaining about is having to do what they were paid to do when they acquired their A paper on the market, namely to honour their commitment to lend. But, having so acquired their A commitments, their status under the facility agreement is as a lender, and the package offers them, if not the certainty, at least the prospect of benefit from its terms. In addition, its terms have improved UPCD's repayment profile, and so in turn have improved the lenders' (including the A lenders') prospects of ultimately being repaid in full. In these circumstances, Mr Onions submits that the claimants have failed to show that the modified waiver letter was incapable of being for the benefit of the lenders as a whole - and the burden of proof is on the claimants to show that the majority lenders' exercise of the clause 25 power was bad.

107. I have noted these points, which I regard as having force, but I am prepared to assume in the claimants' favour that they are right that, at least viewed objectively, the modified waiver letter cannot be said to have conferred a like benefit on all lenders, and that it can be regarded as having ostensibly discriminated against that small sub-class of A lenders who became net payers. In some cases, the demonstration of such discrimination might justify an inference that the exercise of the power had been motivated by improper considerations that ought to vitiate it. But every case turns on its facts, and I am unable to accept that any such inference is justified in this one.

108. The key point in this case is that the claimants' complaints seem to be founded on the premise that the majority lenders had a free hand as to the terms of the modified waiver letter; that they could and should have recognised the disadvantages to which it subjected a small sub-class of A lenders; and they should have somehow (precisely how is not identified) devised a different scheme which treated everyone equally. The fallacy in this is that the majority lenders did not hold all the cards and did not have such a free hand. The modified waiver letter represented the fruit of an arm's length negotiation between TD Bank and UPCD. I find that those negotiations were not easy, and UPCD was not prepared to give the lenders precisely what they wanted. TD Bank could not simply dictate the terms: UPCD could have called the lenders' bluff and invited them to realise their securities. One thing the lenders did want was an. overall reduction in the facility, and assumed it would be in its undrawn elements. In the first instance, UPCD would not agree to any reduction, and required that any discussions on the subject had to be with UGC. Although UGC then agreed to a Euro 500m reduction, it also insisted that UPCD should decide how it should be allocated. This was an understandable condition, since UPCD had to be able to satisfy itself how it could accommodate a Euro 500m reduction within its cash requirements. UPCD did decide on the method of allocation, and the result was the scheme contained in the modified waiver letter, being an allocation between two of the three facilities, which it regarded as the optimal one for its own cash flow purposes.

109. Now it would seem to me that, in this particular context, the optimal allocation from UPCD's viewpoint was likely also to be the optimal allocation from the lenders' viewpoint. The allocation worked out by UPCD was that which gave it the best chance of survival, and Mr Brisby's stance in his cross-examination of Mr Okhuijsen was that it was the only allocation to which it could agree. Mr Okhuijsen. did not regard the matter quite so inflexibly, and indicated that, had the C lenders insisted on a share of the reduction, he could have accommodated them, but that is not what he wanted, and in the event the C lenders did not ask for a share.

110. The result, therefore, was that what was put to the lenders on 4 September was an allocation on which UPCD was insisting. It had not been pre-determined by TD Bank, the CCL or any of the lenders, and any suggestion that the lenders or any of them in some manner fixed it so that the B lenders could benefit at the expense of the A lenders is unfounded (in fact, only 14 out of the 29 B lenders so benefited: on others the effect was either neutral, or else they were net payers). The claimants' complaint, as repeatedly expressed in the oral evidence of Mr

Wilkinson, their solicitor (none of the individuals behind any of the claimants gave evidence) was that the allocation involved the making by the A lenders of advances to pay B lenders. The allocation did involve that, and it can be said to have had an ostensible adverse effect on that small minority of A lenders which became net payers. But that adverse effect was simply part of the price of achieving the overall facility reduction which was for the benefit of all lenders, including the A lenders. The existence of such an effect does not, in my view, automatically undermine the fairness of the reduction scheme as a whole, nor does it cause it fall outside the purpose of the clause 25 power. Nor, in my view, does the exercise of the power become bad because it was necessary, in order to implement the proposed reduction, for the majority lenders also to amend the covenants so as to enable UPCD to make the required draw down. That was simply part of the mechanics necessary to achieve the reduction.

111. Two further points need to be made about the allocation as between the A and B lenders. First, complaint is made that the A facility was reduced by only 11.07% whereas the B facility was reduced by 15.16%. That is said to be manifestly discriminatory and unfair. In my view, this point is not well founded. The explanation for the difference is that it was a necessary consequence of UPCD calculation of the optimal allocation. It was not being imposed on the A lenders by the majority lenders, it was in effect being imposed on all the lenders by UPCD. Equality across the board was not the exercise that UPCD was trying to achieve; it was trying to achieve the optimal method of effecting the overall reduction, being a reduction which would benefit all lenders. In particular, the C lenders were given no reduction at all, but they raised no objections and a majority of them consented to the modified waiver letter. The short explanation for the disparity between the A and B lenders in this respect is that UPCD was calling the tune on this aspect of the waiver,, and whilst (for its own good commercial reasons) it was prepared to agree to unequal reductions as between the three lending classes, it was not prepared to agree to equal reductions. It is possible that, had the CCL gone back to UPCD, it might have been able to persuade it to agree a different allocation, although this would not have been as beneficial to UPCD - and it was important that UPCD had a repayment profile which it could meet. The agreement of the majority lenders to this particular disparity as part of the means of achieving the overall reduction was, in my view, a commercial decision to which they were perfectly entitled to come, and it was one which I consider was within the scope of the power conferred on them by clause 25. Mr Brisby's submission that this disparity was, by itself, manifest discrimination entitling the claimants to succeed is one which I am unable to accept. It can only be advanced on the basis that clause 25 requires the waiver and amendment powers to be exercised equally across the board as between all three classes of lenders. In my judgment, that approach to clause 25 involves subjecting it to restrictions which it cannot fairly bear.

We have been considering the relationship between contracts and tort and fiduciary duty. The Delaware Chancery Court addressed this issue in *Abry Partners V, LP v F&W*

Acquisition LLC.[40] The contract (a stock purchase agreement) limited liability in relation to representations in the contract (the contract established an indemnity fund and limited liability to the amount of the fund). The purchaser alleged the existence of a scheme to manipulate the financial statements of the acquired entity to increase the purchase price. Vice Chancellor Strine declined to enforce the contract as written:

For reasons I explain, I conclude that Delaware law permits sophisticated commercial parties to craft contracts that insulate a seller from a rescission claim for a contractual false statement of fact that was not intentionally made. In other words, parties may allocate the risk of factual error freely as to any error where the speaking party did not consciously convey an untruth. In that context, there is no moral imperative to impinge on the ability of rational parties dealing at arms-length to shape their own arrangements, and courts are ill-suited to set a uniform rule that is more efficient than the specific outcomes negotiated by particular contracting parties to deal with the myriad situations they face.

But the contractual freedom to immunize a seller from liability for a false contractual statement of fact ends there. The public policy against fraud is a strong and venerable one that is largely founded on the societal consensus that lying is wrong. Not only that, it is difficult to identify an economically-sound rationale for permitting a seller to deny the remedy of rescission to a buyer when the seller is proven to have induced the contract's formation or closing by lying about a contractually-represented fact.

For these reasons, when a seller intentionally misrepresents a fact embodied in a contract — that is, when a seller lies — public policy will not permit a contractual provision to limit the remedy of the buyer to a capped damage claim. Rather, the buyer is free to press a claim for rescission or for full compensatory damages. By this balance, I attempt to give fair and efficient recognition to the competing public policies served by contractual freedom and by the law of fraud.

Why is fraud an exception?

The Vice Chancellor also made some comments about the impact of contracting on liability in tort which are relevant to the Armco case (which we will be reading):

Parties operating in interstate and international commerce seek, by a choice of law provision, certainty as to the rules that govern their relationship. To hold that their choice is only effective as to the determination of contract claims, but not as to tort claims seeking to rescind the contract on grounds of misrepresentation, would create uncertainty of precisely the kind that the

[40] http://courts.delaware.gov/opinions/(xjdlbg2orlgze345sjcd0quc)/download.aspx?ID=72140

parties’ choice of law provision sought to avoid. In this regard, it is also notable that the relationship between contract and tort law regarding the avoidance of contracts on grounds of misrepresentation is an exceedingly complex and unwieldy one, even within the law of single jurisdictions. To layer the tort law of one state on the contract law of another state compounds that complexity and makes the outcome of disputes less predictable, the type of eventuality that a sound commercial law should not seek to promote.