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Contentious Commentary

A review for litigators

Contract

Limited vision

The fact that a contract is void does not mean that its performance cannot provide consideration for restitutionary purposes.

Sharma v Simposh Ltd [2011] EWCA Civ 1383 is a case about real property. But it might have reached a more convincing answer if the court had lifted its collective eyes from the cases solely dealing with land and looked at the wider restitutionary picture, for it was on restitution that the case turned.

C and D entered into an oral agreement that, in return for C paying a deposit, D would take a property off the market and sell it to C at a fixed price. C paid the deposit, but later decided not to go ahead with the purchase. She tried to get her deposit back on the ground that the contract was for the disposition of an interest in land, the contract was not in writing and, as a result, the contract was void (not just unenforceable) by virtue of section 2 of the Law of Property (Miscellaneous Provisions) Act 1989.

The Court of Appeal dismissed the claim. Most of the judgment was taken up by a discussion of a couple of confusing and, ultimately, irrelevant Court of Appeal decisions about deposits for real estate transactions before the Court of Appeal concluded succinctly that C was really bringing a restitutionary claim for total failure of consideration, and that the consideration had not totally failed. D had done what it said it would do, ie it had taken the property off the market and was prepared to sell it to C at the price agreed. C had available to her what she had bargained for. Performance of the void contract was consideration for restitutionary purposes, so D could keep the deposit.

The problem was that the Court of Appeal did not survey the restitutionary scene beyond real estate. There was no mention of the local authority swaps cases, in which restitution was granted on both partially and wholly performed interest rate swaps that were subsequently held to be void. The judgments in those cases were given on the basis that the parties did not get what they wanted, ie legally enforceable rights, and therefore there was no consideration (eg *Westdeutsche Landesbank v Islington* [1994] 1 WLR 938). The swaps cases have met with academic criticism, but the Court of Appeal in *Sharma* needed to explain them away in order to reach its judgment. Hunkering down in the real estate silo has merely created problems for the future.

Defining the problem

Acceptance of a repudiatory breach does not allow a contract to be treated as if it never existed.

Contract law is an entirely man-made construction. Unlike gravity, there is no reason inherent in nature why it should be as it is (if there were, English law would be the same as French law, which would be the same as German law etc), but we should at least try to ensure that the structure we have built is coherent and consistent. That sometimes means going back to the basics, and that is where C and the first instance judge failed in *Howard-Jones v Tate* [2011] EWCA Civ 1330. The Court of Appeal was able to correct the position, which is, after all, what it's for.

C agreed to buy real estate from D. The terms required D to install separate water and electricity supplies within six months of completion. The sale completed, title was transferred to C, but D failed to arrange the utilities. After making time of the essence, C purported to give notice “rescinding” the contract and demanding the return of the purchase price (against reconveyance). C then sued for the purchase price.

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The first instance judge recognised that D could not have rescission. Rescission is a remedy for, eg, mistake, misrepresentation or some other factor that vitiates the existence of the contract. On rescission, the contract is treated as if it had never existed, and the parties are put back in the position they were in before the contract (see, eg, *Johnson v Agnew* [1980] AC 367). The remedy is a form of restitution.

Rescission is not available for breach of contract because claiming breach of contract relies on the contract's existence, which cannot therefore be treated as if it didn't exist. Acceptance of repudiatory breach leaves in place accrued rights and obligations, but terminates future primary obligations, replacing them with a secondary obligation to pay damages. (Just to keep everyone on their toes, some older cases do, however, refer to rescission when they clearly mean acceptance of a repudiatory breach. And yes there is also a category of restitutionary damages for breach of contract, but that is a limited and, here, irrelevant exception: eg Treitel, para 20-030.)

Breach of contract leads to a claim in damages. The purpose of contractual damages is to put the parties in the position they would have been in had the contract been performed. At this point, the first instance judge went wrong. Having rightly ruled out rescission, the remedy the judge then granted was restitution, ie return of the purchase price plus additional payments (eg survey fees) against reconveyance of the property.

However, as the Court of Appeal pointed out, that did not put the parties in the position they would have been in had the contract been performed but, instead, in the position they would have been in had it not been entered into, ie as if the contract had been rescinded. The Court of Appeal acknowledged that since C had accepted D's repudiatory breach of the contract, D no longer had an obligation to install the utilities. The measure of damages was the cost to C of doing that work himself, plus ancillary foreseeable losses.

Repudiatory breach does not enable the innocent party to escape the contract as a whole, much as it might want to do so. To be fair to the first instance judge, he was led astray by an earlier and rather confusing Court of Appeal decision (*Gunatunga v DeAlwis* (1996) P&CR 161), but confusion is often best addressed by going back to the basics.

Keeping the right company

Implied term prevents frustration of a valuation procedure.

Cream Holdings Ltd v Davenport [2011] EWCA Civ 1287 is the latest instalment of a long-running dispute. A director/shareholder was sacked and, as a result, provisions in the company's articles were triggered that gave the remaining shareholders the option to buy his shares at a fair value. Seven years and two trips to the Court of Appeal later, this still hasn't happened.

The current position is that, under the articles, an accountant has been nominated by the President of the ICAEW to value the shares as an expert. The accountant requires the terms of his appointment to be agreed by the parties. The ex-director won't agree to them. Does that stymie the process?

Not according to the Court of Appeal. Having accepted that the expert could not just be appointed and that the parties were required to agree his terms, the Court of Appeal was faced with the argument that the procedure was an agreement to agree and, as such, unenforceable. The Court of Appeal circumvented this by implying a term that it was for the expert to put forward his terms of appointment, which the parties could not then unreasonably agree to sign. The parties were not required to agree anything, but could not unreasonably reject the expert's terms.

It may be worth looking at similar provisions closely to ensure that they are on the right side of the line.

Reasonable refusal

The threshold for a reasonable refusal of consent is not high.

Contracts often provide that consent must not be unreasonably refused to a particular course of action. There is little authority in the purely commercial sphere as to what this means, but much more in landlord and tenant cases. All will depend upon the facts, but in *Porton Capital Technology Funds v 3M UK Holdings Ltd* [2011] EWHC 2895 (Comm), Hamblen J accepted that the landlord and tenant cases "provide some assistance" and, in particular, that:

- the burden of proof is on the person seeking to show that a refusal of consent is unreasonable
- it is not necessary for the person who refused consent to show that the refusal was right or justified, simply that it was reasonable in the circumstances
- in determining what is reasonable, the person whose consent is sought is entitled to have regard to its own interests
- the person whose consent is sought is not required to balance its interests against those of the other party, or to have regard to costs that the other might incur if consent is refused.

The message seems to be that it will generally be pretty hard to show that consent has been unreasonably refused - but beware of the facts.

Sovereign immunity

The statute of uses

A debt owed to a sovereign is not in use for commercial purposes.

Section 13 of the State Immunity Act 1978 provides that property owned by a state is immune from enforcement, but section 13(4) goes on that this immunity does not extend to "property which is for the time being in use or intended for use for commercial purposes". But what if the property is a debt? What is a debt used for? Do you look to the transaction that led to the debt or to the use to which the money will be put if the debt is paid? In *Servaas Inc v Rafidain Bank* [2011] EWCA Civ 1256, the Court of Appeal (by majority) went for the latter.

C secured a French judgment against Iraq, which it sought to enforce by means of a third party debt order over a dividend to be paid to Iraq by Rafidain Bank's London Branch (in provisional liquidation and with a scheme of arrangement in place) . The dividend was due to Iraq because Iraq was the assignee of commercial debts owed by Rafidain, largely on letters of credit issued by the bank. Iraq bought these debts at 10.25% of face value as part of its settlement of Saddam-era debts owed by the Iraqi public sector, including by Rafidain. The dividend to be paid by Rafidain to Iraq was 53% of face value.

Stanley Burnton and Hooper LJJ concluded that the debt owed by Rafidain was not currently in use at all. It was the equivalent of a dormant bank account. Once paid, the proceeds were, it was agreed, to be used for sovereign, not commercial, purposes. Section 13(4) did not therefore apply, and the third party debt order could not be made absolute. Hooper LJ added that, in his view, the underlying commercial nature of the debts was irrelevant, but the purpose of Iraq's acquisition of those debts might be relevant. If so, he thought that acquisition of the debts was for a sovereign rather than a commercial purpose. He didn't say what that sovereign purpose was.

Rix LJ dissented. He considered that the debt owed by Rafidain to Iraq was currently in use by Iraq. That use was to convert it into cash as part of a commercial transaction under which Iraq bought the debts for a knock-down price and secured payment, realising a profit. Iraq was simply the holder of a commercial debt like anyone else, and could not claim sovereign immunity to prevent enforcement against the debt.

The difficulty with the majority's approach is trying to work out how far it goes. Does it mean that a sovereign can always say that a debt is not in use (eg it is not being assigned) and that the proceeds of the debt will be used for sovereign purposes? Or does it only mean that in the rather peculiar circumstances of Iraq and Rafidain, this holds good but will not do so in other more usual situations? The danger is that the majority view might give sovereigns too much leeway in resisting enforcement. And there is, perhaps, a risk of this mattering more in the future than it has in the past.

Rome II

Time and time again

The Rome II Regulation applies to events giving rise to damage that occurred after 11 January 2009.

Article 31 of the Rome II Regulation states that the Regulation (which determines the law governing non-contractual claims) applies to events giving rise to damage which occur after its entry into force. The Regulation did not say expressly when it was to come into force. As a result, what is now article 297 of the Treaty on the Functioning of European Union applies, and Rome II came into force 20 days after its publication on the Official Journal, ie on 20 August 2007.

Article 32 of the Regulation goes on to state that the Regulation applies from 11 January 2009. It thus draws a distinction, well-known in EU law, between entry into force and application. Unfortunately, in this context the result is incoherent. It seems to mean that Rome II applies to an event giving rise to damage that occurred in, say, September 2007 (article 31), but that the courts do not have to apply the Regulation unless they are sitting after 11 January 2009 (article 32; see Dickinson, *The Rome II Regulation*, paragraph 3.315ff).

This is a legislative oversight. The underlying issue is how far courts can go to put it right – where does the judicial role end and the legislative role begin? As one might expect, in *Homawoo v GMF Assurances SA* (Case C-412-10) the Court of Justice of European Union decided that the courts have a long reach when it comes to correcting the legislators' mistakes. The CJEU concluded that, in context, Rome II only applies to events giving rise to damage that occur after 11 January 2009. That is not what the Regulation says, and the CJEU's reasoning is rather thin. But it is what the EU legislators ought to have provided had they addressed the point, and so it was what they were interpreted as having provided.

Conflict of laws

Staying put

English proceedings are not stayed because of related Greek proceedings.

Some English judges are wary about being seen to promote the English courts too much. But some, even if sotto voce, recognise that there is benefit for the British economy and the maintenance of judicial employment in encouraging international litigation in this country, not least in these straightened times, and recognise their role in securing those ends (see Vos J's KPMG speech of 18 October; see also the letter from the Chairman of the City of London Law Society to the Financial Times on 25 November 2011 on the economic benefits of Messrs Beresovsky and Abramovich's extensive occupation of the new Commercial Court building). Gloster J is one of those such judges.

She demonstrated this in *Seven Licensing Co SARL v FFG-Platinum IP Rights Ltd* [2011] EWHC 2967 (Comm). The case involved an application under article 28 of the Brussels I Regulation to stay proceedings England in favour of Greece. Article 28 gives the court second seised a discretion to stay its proceedings if its proceedings are related to proceedings in the court first seised. Related for these purposes means that the two proceedings give rise to the risk of conflicting judgments.

The facts of *Seven Licensing* are complicated, but essentially the Greek proceedings involved litigation to restrain a bank from paying on an letter of credit (interim injunctions had been granted), and the English proceedings involved the underlying dispute. It is the factors that Gloster J took into account in exercising her discretion that are interesting. She pointed out that the Greek proceedings were not concerned with the entire dispute and did not include all the parties, but they did clearly overlap with the English proceedings. She went on to take into account in exercising her discretion that the underlying dispute was governed by English law and was subject to English jurisdiction clauses, that some of D's arguments were pitiably weak, and that it would take the Greek courts until at least 2014 to reach a decision, whereas the Commercial Court could do it in the first half of 2012. She therefore decided to stay the English proceedings.

Of course, Gloster J couldn't possibly say that the English courts are quicker and more effective than other courts, so everyone should come to England – judicial comity would prevent the idea of any such a crude marketing ploy even flickering across the judicial brow. But some may read her judgment as leaving behind a Cheshire Cat-like grin to that effect.

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