

The status of multilateral financial institutions in English law

Dealing with a multilateral financial institution raises different issues from transactions with private sector entities. This requires an understanding of the particular institution in question, including its immunities, if any, and its capacity, but there will seldom be insuperable problems.

Multilateral international financial institutions (IFIs) formed by sovereign states play an increasing role in the financial world. These IFIs include, for example, the African Development Bank, the Asian Development Bank, the Caribbean Development Bank, the Inter-American Development Bank, the International Bank for Reconstruction and Development, the European Bank for Reconstruction and Development, the European Investment Bank, the Multilateral Investment Guarantee Agency and, most recently, the Asian Infrastructure Investment Bank.

The involvement of IFIs in financial transactions can arise from their providing finance directly, their providing guarantees to other financial institutions, or their hedging currency, interest or other exposures that they face as a result of their other activities.

This greater role of IFIs, and, in particular, the contracts they regularly enter into with private sector financial institutions, focuses attention on their legal status - indeed, whether they exist at all for national law purposes - and what, if any, immunities they have. In this briefing, we look at the status of IFIs in English law and the issues that dealing with them can bring.

The nature of IFIs

IFIs are commonly formed by an agreement (or treaty) between sovereign states. So, for example: the European Bank for Reconstruction and Development was established in 1991 by an agreement that now has 65 states as members, plus the EU and the European Investment Bank; the African Development Bank was established under an agreement that came into force in 1964 and currently has 78 member states; the Asian Development Bank was established by a charter entered into in December 1965, and currently has 67 member states; and the Caribbean Development Bank was established by a charter of October 1969, and now has 28 member states. All these agreements provide for the institutions they establish to have legal personality, including the ability to enter into contracts and to sue and be sued, but also to have certain immunities from normal legal process.

Agreements of this sort between sovereign states operate in the realm of public international law. This is a distinct realm from the private, or domestic, law that governs most financial transactions (eg English and New York law). The manner of interaction between public

Key issues

- IFIs are increasingly involved in financial transactions
- Dealing with IFIs raises a different set of issues
- The issues include an IFI's status in private law and its immunities
- IFIs may not be subject to any insolvency regime

international law and private law varies between legal systems, but the English legal system adopts a "dualist" approach. This means that an agreement operating at the level of public international law, whether or not the UK is a party to the agreement, gives rise to no rights or obligations under English domestic law unless domestic law measures are taken to give the agreement effect in domestic law.

With regard to IFIs specifically, the dualist approach means that an IFI will not exist so far as the English courts are concerned merely because a treaty says that it exists. An IFI will only be regarded by the English courts as having come into being and as having the corporate capacity to enter into contracts and to own assets if it has been given that capacity by

domestic law. This may occur in one of two ways: by virtue of statute; or under the common law.

Statutory recognition of IFIs

An example of an IFI with specific statutory recognition is the International Monetary Fund. The IMF was established in public international law by the Bretton Woods Agreement of 1944 and was then given legal status in UK domestic law by (originally) the Bretton Woods Agreements Act 1945. An Order made under that Act gave express legal effect to the provision of the Agreement (article IX) that provides for the IMF to "possess full juridical personality and, in particular, the capacity... to contract... [and] to institute legal proceedings" (this Order now takes effect under the International Monetary Fund Act 1979). As a matter of English domestic law, the IMF therefore exists and can enter into contracts because the UK's Parliament – the ultimate source of UK law – has said that the IMF exists.

IFIs are still sometimes recognised in UK law by specific legislation (eg the Multilateral Investment Guarantee Agency, established under an agreement entered into in 1987, was accorded legal status by the Multilateral Investment Guarantee Agency Act 1988). More usually, however, an IFI is recognised as a result of an Order in Council made under the International Organisations Act 1968. That Act allows the UK government to make Orders conferring on IFIs the legal capacity of a body corporate. As a result of this conferral, these IFIs become recognised in English domestic law, with the ability to enter into contracts

and to sue and be sued in the English courts (subject to any immunities, discussed below). Over 80 IFIs have been accorded legal status under the International Organisations Act 1968, including the African Development Bank, the Caribbean Development Bank and the Asian Infrastructure Investment Bank.

Common law recognition of IFIs

The International Organisations Act 1968 applies principally to international organisations of which the UK is a member or which intend to maintain an establishment in the UK. This limit on the scope of the Act therefore leaves a significant number of IFIs that will, potentially, not be recognised by virtue of statute in the English courts. These include the Arab Monetary Fund and OPEC. The UK Government has little incentive to take statutory measures in order to give legal recognition to an IFI of which the UK is not a member or which has no presence in the UK.

Fortunately, however, common law has intervened to accord recognition to most of these IFIs by using an analogy with the position at private law. Companies incorporated under a foreign state's private law are recognised within the UK as having legal personality. The English courts merely look to see whether the entity has been incorporated under the private law of a foreign state; if it has, it will be recognised in the English courts. A similar approach is taken to IFIs. The question is whether the IFI has been accorded the legal capacity of a corporation under the domestic law of any of the IFI's member states or, if different, the law where the IFI has its seat. Where this has been done, the English courts will similarly

treat an IFI as having the legal capacity of a corporation in the same way that the English courts recognise entities formed more conventionally under foreign corporate law.

IFIs – at least those that have a physical presence – will commonly enter into a headquarters agreement with the state in which the IFI is to be based. This agreement will usually accord the IFI corporate capacity as a matter of local domestic law so that the IFI can acquire property, employ staff and so on. This will be sufficient for the English courts to recognise the existence of the IFI. Even if there is no headquarters agreement, if the treaty under which the IFI is established grants legal capacity to the IFI and the treaty is effective in a member state's domestic law to accord legal capacity to the IFI, that will again be sufficient for the English courts.

Accordingly, despite the theoretical issues surrounding the recognition of IFIs as a matter of English law, in practice there is unlikely to be any difficulty in the vast majority of cases.

Vires

The capacity of a commercial entity to enter into a particular transaction is now seldom a problem, though it can still be relevant for the public sector. However, it could be an issue for an IFI. The primary question – whether the IFI has the capacity to enter into the transaction – is likely to be a matter of the interpretation of the agreement under which the IFI was established and any other relevant documents. This will not be governed by English law, New York law or any other domestic law but by public international law, in practice as reflected in the Vienna Convention on the Law of Treaties. This can lead to

greater ambiguity than is usually the case in private law if an IFI is entering into a transaction of a sort that is not clearly permitted by its founding treaty.

English private law has traditionally taken the strict approach that ultra vires arrangements are void (ie of no legal effect), thus placing the risk of ultra vires on the counterparty. Whether this same approach would or should be applied to IFIs is unclear. As a result, the consequences of an IFI acting outside its powers are uncertain.

Immunities

If an IFI is recognised under statute, the statute will generally grant some form of immunity from the jurisdiction of the English courts. In particular, section 1(2) of the International Organisations Act 1968 allows Orders in Council made under its terms to provide immunities to an IFI, but the extent of the immunities will depend upon the underlying treaty. So, for example, the IMF and the OECD and their respective assets have wide-ranging immunity from legal process, but the International Finance Corporation and the European Bank for European Reconstruction and Development have more limited immunity, doubtless in recognition of the fact that they are intended to enter into transactions with private sector entities and must, therefore, play by private sector rules - to some extent at least. The extent of any immunities will vary from organisation to organisation.

An IFI can in general expressly waive in a contract some or all of the immunity it might otherwise have.

If an IFI is only recognised under English common law, it is unlikely that the IFI will have any immunity as a matter of English law.

Any immunity that an IFI may have will in general only be from the jurisdiction of the English courts, whether that jurisdiction is to determine liability or to enforce a resulting judgment. If a financial institution holds security for the obligations of an IFI or is entitled by contract to set off various liabilities without recourse to the courts, immunity from jurisdiction will not be relevant. The financial institution can exercise its contractual rights without needing any sanction from the court. If the IFI wishes to challenge the financial institution's conduct, the IFI must go to court, which will generally result in the waiver by the IFI of whatever immunity it might otherwise have had in respect of the claim.

Insolvency

The English courts have jurisdiction under the Insolvency Act 1986 to wind-up certain "unregistered companies", which can include companies incorporated outside the UK. However, this does not confer jurisdiction to wind-up IFIs. The English courts have taken the view that Parliament cannot by mere general words have intended the English courts to enforce obligations between sovereign states and otherwise to interfere in the running and administration of an IFI in the way that would necessarily result from insolvency proceedings.

As a result, if an IFI becomes insolvent, the creditors have no recourse to the English courts to initiate any form of collective insolvency proceedings (though it is unclear whether an English court would give effect to insolvency proceedings in another court). The contract with the IFI will remain valid, and creditors will still be able to take steps to enforce the contract through

the seizure of security and other assets within the creditors' control or, if permitted, by court action against the IFI's other assets. Creditors of the IFI might find themselves in a race to identify and seize the IFI's assets.

Netting

If a financial institution proposes to enter into a number of transactions with an IFI, the parties may agree to net some or all of their resulting mutual liabilities. Netting could be of importance, for example, to reduce risk for regulatory capital purposes. Where Regulation (EU) No 575/2013 on prudential requirements for credit institutions (the CRR) applies, article 296 requires financial institutions to have legal opinions to the effect that, in the event of legal challenge, the financial institution's claims and obligations would not exceed the net sum of the positive and negative mark-to-market values of individual transactions. The legal opinions must cover the law that applies to the individual transactions and to the agreement that permits netting, and also the law of "the jurisdiction in which the counterparty is incorporated".

If the transactions in question and the netting agreement are governed by English law, the fact that the transaction is with an IFI should not adversely affect the operation of the netting provisions for the reasons given above. What may be more complicated is addressing the requirement for a legal opinion regarding the jurisdiction in which the IFI is incorporated. An IFI is not incorporated as such in any jurisdiction but as a result of an agreement taking effect in public international law. English courts might recognise the existence of an IFI, whether under statute or at

common law, but that does not mean that the IFI is incorporated in England. The jurisdiction that probably best corresponds to the place of incorporation for this purpose is the location where the IFI is headquartered (and, if a separate branch of the IFI is involved, the location of that branch). It may therefore be that (at least) two opinions are required: one relating to the governing law of the netting agreement and the underlying transactions; and the other relating to the place where the IFI is headquartered.

Conclusion

Dealing with IFIs brings with it problems not present in transactions with private sector entities. Those problems are, however, seldom insuperable.

Contacts

Deborah Zandstra
Partner

T: +44 20 7006 8234
E: deborah.zandstra@cliffordchance.com

Simon James
Partner

T: +44 20 7006 8405
E: simon.james@cliffordchance.com

Habib Motani
Partner

T: +44 20 7006 1718
E: habib.motani@cliffordchance.com

Andrew Yianni
Consultant

T: +44 20 7006 2436
E: andrew.yianni@cliffordchance.com

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Clifford Chance, 10 Upper Bank Street, London, E14 5JJ
© Clifford Chance 2017

Clifford Chance LLP is a limited liability partnership registered in England and Wales under number OC323571

Registered office: 10 Upper Bank Street, London, E14 5JJ

We use the word 'partner' to refer to a member of Clifford Chance LLP, or an employee or consultant with equivalent standing and qualifications

If you do not wish to receive further information from Clifford Chance about events or legal developments which we believe may be of interest to you, please either send an email to nomorecontact@cliffordchance.com or by post at Clifford Chance LLP, 10 Upper Bank Street, Canary Wharf, London E14 5JJ

Abu Dhabi • Amsterdam • Bangkok • Barcelona • Beijing • Brussels • Bucharest • Casablanca • Dubai • Düsseldorf • Frankfurt • Hong Kong • Istanbul • Jakarta* • London • Luxembourg • Madrid • Milan • Moscow • Munich • New York • Paris • Perth • Prague • Rome • São Paulo • Seoul • Shanghai • Singapore • Sydney • Tokyo • Warsaw • Washington, D.C.

*Linda Widyati & Partners in association with Clifford Chance.

Clifford Chance has a best friends relationship with Redcliffe Partners in Ukraine.

Clifford Chance has a co-operation agreement with Abuhimed Alsheikh Alhagbani Law Firm in Riyadh.