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LMA Briefing Q4 2018

In this briefing, Brian Cain, a solicitor in the LexisPSL Banking & Finance team, looks at a trade finance case *Cargill International Trading Pte Ltd v Uttam Galva Steels Limited* [2018] EWHC 2977 (Comm). A seller of steel had received advance payments under a number of sale and advance payment facility agreements and later disputed that those payments were properly due to be repaid in accordance with the terms of the documents.

Cargill International Trading Pte Ltd v Uttam Galva Steels Limited [2018] EWHC 2977

This method of finance had been used by the parties over a number of years to fund the seller's working capital requirements. When the steel market hit problems because of world wide oversupply the seller became financially distressed. The buyer/funder wanted to reduce its credit risk by asking the seller to repay the outstanding US$ 61.8 million advances in full rather than extending the facility for a further period.

Why is the case of interest?

Although the *Cargill* case involved advanced payment facilities relating to the supply of steel the terms of the sale and finance agreement contained provisions which are similar to those found in loan agreements used widely in the market and designed to protect lenders from claims that payments can be reduced or delayed by counterclaims from a borrower.

The case looked at whether the buyer who made the advance payments and so was in a position similar to a lender:

> was obliged to roll over the facility (providing a new facility to allow repayments of an old facility) as it had done for a number of years prior to the dispute arising;

> could rely upon protective clauses in the facility agreements which stated that the seller's payment obligations remained in effect notwithstanding any breach of the agreement by the buyer; and

> whether the "prevention principle" applied to prevent the buyer enforcing rights.

The "prevention principle" relates to a situation where one party by its own breach of contract prevents the other contractual party from complying with its obligations under that same contract.

The principle operates to stop the first party from enforcing its rights. Its deployment as a defence in the context of a financing agreement was unusual and as discussed below ultimately unsuccessful.

The facts

Cargill bought steel from Uttam. It did so under the facility agreements which were contracts for the sale and purchase of steel with a financing arrangement coupled to the sale contract. Under the facility agreements Uttam could ask Cargill to make advance payments which if approved by a credit committee at Cargill would be funded for 180 or 360 days. Cargill had two facilities in place and US$61.8 million outstanding under them at the relevant time.

Uttam could repay the advance payments in three ways:

> by delivering steel to Cargill

> by delivering steel to a third party nominated by Cargill; and

> by paying cash to Cargill

If the first or second method were used Uttam had to send a document called an "Offer to Purchase" to Cargill with the stated value of the steel which Cargill could either accept or refuse.

Under the facility agreements the offer was stated to be valid for 7 days during which time Cargill "may either accept ... or may decline ... in writing". Only if Cargill accepted and the steel was supplied would the amount due to Cargill be satisfied in whole or part by the stated value of steel delivered under the Offer to Purchase.

Cargill could always insist upon repayment of advances made to Uttam in cash on the due date. The agreements between the seller and buyer left the decision as to which method was acceptable in the hands of Cargill.

The parties had a long history of trading. Throughout that history it was common for Uttam to pay to Cargill outstanding sums that would otherwise have to be paid in cash (rather than the delivery of steel) from the proceeds of advanced payments generated under a new facility agreement entered into with Cargill at the time an old liability matured. This "rolling over" of liability was a key element in maintaining Uttam's cash flow over the previous decade or more. It was also at the heart of Uttam's arguments that it was not liable to repay the advanced payments made by Cargill at the point the dispute arose.

The falling demand for steel and a general over-capacity in the steel producing market conspired to undermine Uttam's financial position. It found itself in severe financial distress. Although discussions took place between Uttam and Cargill over the possibility of new advances being made they were at a relatively early stage. As those discussions took place several payments matured becoming due to Cargill. As a result of Uttam's troubled financial position those repayments were never made. Cargill's credit committee subsequently turned down Uttam's request for a new facility – partly because of this default - and Cargill sued for the entire amount previously advanced by it to Uttam.

Was Cargill obliged to roll over the debt?

Uttam stated in its Defence that Cargill "had always refreshed or provided new facilities since 2005". This had allowed Uttam to use the proceeds of the new advance payments to repay prior advance payments outstanding and due at the time the new facility agreement was entered into. Uttam pleaded (though from the judgment it appears not in a terribly detailed fashion) that there was a common assumption by both parties that this was a state of affairs that would continue. That, Uttam argued, led to an estoppel by convention which prevented Cargill from denying that state of affairs would continue. If this argument was successful it followed – at least to Uttam's mind – that Cargill was prevented from enforcing its rights to repayment under the existing facility agreements.

The judge was not impressed by this line of defence.

It was a fact that the proceeds of a new advance payment facility had been used to repay a sum due under an older facility several times in the past. Cargill had acknowledged this historical practice in e-mails flowing between the two parties during the discussions on a possible new facility. The key email from Cargill relied upon by Uttam stated:

"With regard to future disbursement as you know we [Cargill] are working on it and cannot give you a concrete date as it is dependent on internal credit and approval processes which is ongoing. We will endeavour to do the best we can as we have in the past. However not receiving a payment on a due date would trigger a default, something we have not seen in our entire relationship over the years and will have a bearing on all our future deals. Hope you appreciate that and make the payment as per the contract..."

The judge thought the evidence was nowhere near enough to establish a common assumption upon which an estoppel could be founded. The emails simply acknowledged a practice that had existed for over 10 years. They provided no reasonable basis for any assumption. Their content was much too general. For example, there was no detail as to the amount or maturity date of any new facility.

Furthermore, the emails clearly showed that Cargill would be putting Uttam's request for a new facility to a credit committee for approval and one factor that committee would consider in making its decision was whether Uttam had defaulted on repayments which had already become due.

The judge considered that this evidence showed the exact opposite of what Uttam was trying to establish. Uttam needed to show that **both** parties were working on the basis Cargill was going make a new facility available. The emails showed Cargill was simply considering whether to do so and that its credit committee had a final say in the provision of any new facility.

Putting a further nail into the coffin of the "estoppel by convention" defence the judge pointed out that no cases dealing with this form of estoppel had been cited that obliged a party to enter into a new agreement. He considered that it was impossible in these kinds of circumstances for an estoppel by convention to operate in this way because in the absence of very specific representations detailing the terms of the new facility the evidence would at most establish only an "agreement to agree". Such an agreement would be not enforceable when detail of important terms such as the amount and maturity date of the advance were missing.

There was no estoppel by convention and Cargill was not obliged to roll over the advance payment facility.

Protective provisions and the "prevention principle"

Uttam's next line of defence was to deploy the "prevention principle".

Uttam argued that it had sent an "Offer to Purchase" for an amount of steel valued at US$6 million to Cargill and that this offer had to be accepted or refused in writing within 7 days. In breach of contract Cargill had neither accepted nor refused the offer.

Quite how this failure if proven relieved Uttam of its repayment obligation in relation to the US$61.8 million was not entirely clear to the judge. No evidence that acceptance of this Offer for Purchase by Cargill would have miraculously cured Uttam's entire cash flow problem allowing it to pay the full amount due was produced. The judge nevertheless dealt with Uttam's argument that this assumed breach by Cargill triggered the "prevention principle" which could in theory have prevented or delayed Cargill from enforcing the right to repayment of the US$61.8 million.

The facility agreements contained certain protective provisions designed to benefit Cargill. These provisions are set out in full in an appendix to the judgment.

The judge rejected this defence for the following reasons:

> Cargill had complete freedom to accept or refuse any future offers made by Uttam and Cargill could not have been forced to accept further deliveries of steel in lieu of cash;

> In fact Uttam made no further Offers to Purchase and did not supply any steel under the US$6 million offer so there was in fact no reduction in its debt;

> Assuming Cargill had breached its contract by neither accepting or rejecting Uttam's offer the facility agreement contained several provisions stating that no breach of the agreement by Cargill would affect Uttam's repayment obligation;

> Cargill had the benefit of a "no set off" provision and there was a long line of cases which established these clauses were enforceable even where a counterclaim was made good;

> Uttam's general argument that these protective provisions offended a general principle that a person should not benefit from his own wrong did not invalidate the provisions;

> The prevention principle had no operation where the contract contained an express term making it clear no breach of the agreement by Cargill would affect the repayment obligations of Uttam

Cargill was given summary judgment for the full amount of its claim.

Lessons for lenders and borrowers

It is not unknown for borrowers to raise the argument that lenders are bound to roll over or renew existing facilities (at least for some period of time) allowing them to delay payment and thus cure any default relating to missing a contractual repayment date. The *Cargill* case suggests that a borrower is going to have to produce evidence of *details* of the new facility - such as amount, cost and maturity as a bare minimum simply to get to the starting post for running that type of argument. Anything less is going to be insufficient and will fail as an agreement to agree. If the lender is making encouraging noises but still makes it clear there are conditions which need to be satisfied there can be no "common" assumption on which to base any estoppel.

Protective provisions mean what they say and "no set off clauses" and similar provisions preventing borrowers from delaying repayment on the basis of counterclaims work.

The so called "prevention principle" has no operation where the parties contract on the basis of these types of protective provisions particularly in a finance context.

As one commentator has put it the leading case on the prevention principle, *Peak Construction (Liverpool) Ltd v McKinney Foundations Ltd* (1970) 1 BLR 111 which involved the construction of flats in Liverpool has:

paved the way for 40 years of conflicting authority and academic comment...[and] to this day, many issues remain unresolved. (The Peak effect - (2011) 22 9 Cons.Law 14)

The prevention principle is probably a defence best left to the construction and other markets where cascade effects from relatively minor breaches is more problematic. In the finance market where certainty of payment obligation is critical it will probably remain of much more limited application. Even in construction contracts where the prevention principle can trace it's origins the recent cases suggest a judicial desire to see proper boundaries laced on the principle so that it operates by way of an implied term in an existing contract rather than an overriding rule of public policy; see *North Midland v Cyden Homes* [2018] EWCA Civ 1744.