EMTV v Bayerische Landesbank

Jurisdiction:	Jersey
Judge:	Bailiff, THE
Judgment Date:	20 February 2003
Neutral Citation:	[2003] JRC 39
Reported In:	[2003] JLR 80
Court:	Royal Court
Date:	20 February 2003

Text

[2003] JRC 39

ROYAL COURT

(Samedi Division)

Before:

The Bailiff, **sitting alone**.

Between
EM TV & Merchandising
Aktiengesellschaft
Plaintiff
and
Bayerische Landesbank
Defendant

and

Speed Investments Limited
First Party Cited

and

SLEC Holdings Limited
Second Party Cited

and

Mourant & Co Secretaries Limited
Third Party Cited

and

JP Morgan Chase Bank
Lehman Commercial Paper Inc
Dr Dietrich Wolf
Dr Rudolf Hanisch
Dr Thomas Fischer
Mr Klaus Diederichs
Mr Thomas Bernard
Intervenors

Advocate F B Robertson **for the Plaintiff**

Advocate M J Thompson **for the Defendant**

And for the Intervenors.

The Parties Cited did not appear and were not represented.

Authorities

Draft Security Interests (Amendment) Jersey Law Projet 5 June 1984.

Macon v Quérée (2001) JLR 80 .

Matthews and Nicolle “The Jersey Law of Property” pp 60 – 64.

Pothier “Traité du Contrat de Nantissement” (1825 ed) volumes 6 and 12 pp 240 – 245 and pp 193 – 194 respectively.

“Chitty on Contracts” (28 th ed) para 12-002.

The Shorter Oxford English Dictionary.

Kaye v Croydon Tramways Company [1898] 1 Ch 358 .

Henderson v Bank of Australasia [1890] LR 45 Ch. D330 .

Re Bridport Old Brewery Company [1866 – 67] LR 2 Ch App. 191 .

Re Green's Will Trusts [1983] 3 All ER 455 .

Ellis v Emmanuel (1875 – 76) LR 1 Ex.D. 157 .

Hobson v Bass (1870 – 71) LR 6 Ch. App. 792 .

Brandao v Barnett (1846) 12 Cl & Fin 787 .

Re United Service Co (1870) 6 Ch App 212 .

Shah v Shah [2002] QB 35 .

Whether to specify an event of default, for the purposes of Article 3(i)(f) of the Security Interests (Jersey) Law 1983, the event of default had to be contained wholly within the Security agreement itself.

Bailiff THE

1 This case raises a short but important point of law involving the construction of the word "specified" in Article 3(1)(f) of the Security Interests (Jersey) Law 1983, as amended ("the Security Interests Law"). Upon this issue turns the validity of a security agreement dated 30th March 2001 by which the plaintiff purported to create a security interest in its shares in Speed Investments Limited ("Speed") to secure obligations and liabilities towards the defendant and two of the intervenors, viz J P Morgan Chase Bank ("JP Morgan") and Lehman Commercial Paper Inc ("Lehman") (collectively referred to as "the banks").

2 The background may for these purposes be shortly stated. Immediately before the security agreement was executed on 30th March 2001 the plaintiff owed 100% of Speed, which in turn owned 50% of SLEC Holdings Limited ("SLEC"), which owns (through subsidiaries) the television rights in Formula 1 motor racing. These rights are very valuable. The plaintiff was, however, in some financial difficulties and early in 2001 negotiated to sell a proportion of its shares in Speed to the Kirch Group, a German media company. Funding for this acquisition by the Kirch Group came essentially from the banks or, in one case, its predecessor in title. The defendant advanced $987.5 million, Lehman advanced $300 million and Kirchmedia (predecessor in title to JP Morgan) $282.7 million, making a total of over $1.5 billion. The arrangements involved the incorporation of a subsidiary of the Kirch Group called Formel Eins Beteiligungs Gmbh ("FEB") to which the defendant, Lehman and Kirchmedia advanced the money. Upon completion of the arrangements, FEB owned 77.7% of Speed and the plaintiff's shareholding had reduced to 22.3%. Speed was, however, enabled to exercise a call-option so as to acquire a further 25% of the shares of SLEC and to increase its shareholding to 75%. The loans by the defendant, Lehman and Kirchmedia were secured, inter alia, by the security agreement referred to in paragraph 1

above (hereafter “the EM TV security agreement”) by which the plaintiff purported to create a security interest over its shareholding in Speed to guarantee (on a limited recourse basis) all monies owing by FEB to the secured creditors (who were, with effect from 17th July 2001) the banks. On 17th July 2001 Kirchmedia's loan had been acquired by JP Morgan. The relationship between the lenders was governed by another agreement dated 30th March 2001 called the “Intercreditor Agreement”. The plaintiff was not a party to the Intercreditor Agreement. The Intercreditor Agreement was amended by a further deed dated 17th July 2001 to the extent necessary to reflect the substitution of JP Morgan as a lender in place of Kirchmedia.

3 There is little doubt that on 30th March 2001 all the parties (including the plaintiff) believed and were advised that the EM TV security agreement was valid. Mr Thompson for the defendant accordingly characterised the proceedings as an unworthy attempt to renege on a commercial agreement by taking advantage of a technical point. Mr Robertson for the plaintiff sought to justify the proceedings on the basis that the banks stood to make a windfall profit as a result of enforcing their alleged security. If that be the case, that was the contractual arrangement into which the plaintiff entered with its eyes open. Counsel's better point in response was that an argument does not become a bad one, merely because it is technical.

4 The plaintiff's case is based upon a short point of statutory construction. Article 3(1)(f) of the Security Interests Law provides that –

> ***“For the purposes of this Law a security agreement shall –***
>
> ***.....***
>
> ***(f) specify the events which are to constitute events of default”*** .

In the submission of counsel for the plaintiff, the word “specify” means that the events of default must be contained within the security agreement itself. He submits that they were not so contained and that the EM TV Security Agreement did not comply with the requirements of the Security Interests Law. It follows, counsel contends, that the security interest over the plaintiff's shares in Speed is invalid.

5 This submission must be considered against the background of an amendment to the Security Interests Law that was enacted in 1985. In its original form article 3 of the Security Interests Law provided –

> ***“Security Agreement***
>
> ***(1) For the purposes of this Law a security agreement shall –***
>
> ***(a) be in writing;***
>
> ***(b) be signed by the debtor; and***

(c) specify –

(i) the name of the debtor;

(ii) the name of the secured party;

(iii) particulars of the collateral sufficient to enable it to be identified;

(iv) particulars of any encumbrances affecting the collateral;

(v) the events which are to constitute events of default; and

(vi) the nature, duration and amount of the obligation payment or performance of which is secured under the security agreement .

(2) Subject to paragraph (1), a security agreement may be in such form and contain or refer to such matters as shall be agreed between the parties to such agreement."

6 By Article 2 of the Security Interests (Amendment) (Jersey) Law 1985, Article 3 of the Security Interests Law was amended by deleting sub-paragraphs (b) and (c) of paragraph (1) and substituting the following sub-paragraphs –

"(b) be dated;

(c) identify and be signed by the debtor;

(d) identify the secured party;

(e) contain provisions regarding the collateral sufficient to enable it to be identified;

(f) specify the events which are to constitute events of default; and

(g) contain provisions regarding the obligation payment or performance of which is to be secured sufficient to enable it to be identified."

It is noted that, whereas the original text required a number of matters to be "specified" in the security agreement, the only matter now required to be "specified" is the events which are to constitute events of default.

7 The question is therefore what "specify" means in the context of the Security Interests Law. Counsel for the plaintiff referred me to the definition of "specify" (as a transitive verb) in the Oxford English Dictionary –

"To mention, speak of, or name (something) definitely or explicitly; to set down or state categorically or particularly; to relate in detail. Usually said of

persons, but sometimes of an act, document, etc."

8 Counsel submitted that a specification must have the relevant detail within itself. He contrasted "specify" (a strong word) with "identify" (a weaker word) in the other sub-paragraphs of article 3(1). He drew some support for this submission from *R v Inland Revenue Commissioners, ex-parte Ulster Bank* [1997] STC 832 at 841 where Morritt J stated in the context of the Taxes Management Act 1970 –

> ***"The word 'described' is wider than the word 'specified'; it connotes the recitation of the characteristics of that which is referred to rather than its details or particulars."***

9 Counsel for the plaintiff referred me to two other cases. In *Re Arthur Average Association for British, Foreign & Colonial Ships* (1875) LR 10 Ch App 542 the validity of certain insurance policies was an issue. Sir G Mellish LJ stated at 549 –

> ***"I am of the opinion that the order of the Master of the Rolls is correct.*** The 7th section of the 30 Vict. c. 23, says: "No contract or agreement for sea insurance (other than such insurance as is referred to in the 55th section of the Merchant Shipping Act Amendment Act, 1862), shall be valid unless the same is expressed in a policy; and every policy shall specify the particular risk or adventure, the names of the subscribers or underwriters, and the sum or sums insured; and in case any of the above-mentioned particulars shall be omitted in any policy, such policy shall be null and void to all intents and purposes." The Legislature, therefore, says, in the plainest possible terms, that the name of the subscribers or underwriters are to be inserted in the policy, and in case that is omitted then the policy is to be null and void to all intents and purposes .
>
> ***The policy in the present case, is signed "per procuration of the several members of the Arthur Average Association for insuring each other's ships, every member bearing his equal portion according to the sums mutually insured."*** There is considerable doubt as to what those words mean, whether they mean what is their natural meaning, that the existing members of the ***Arthur Average Association, each in proportion to the sum for which he is insured, are to be the underwriters of this policy or whether they mean what, if you are to import the rules of the Arthur Average Association, they must have been intended to mean – not the persons who are the members at the time when the policy is executed, but the persons who are the members at the time the loss accrues, because those are the persons who are liable according to the rules.*** If a man insures for a year, when his year is over he is not liable for any loss which occurs afterwards. It appears to me to be unnecessary to decide which of those two constructions is right, because whichever of them is right, I entirely agree with the Master of the Rolls that the requisition of the statute is not complied with. …… In this case there is an insurance by which every member is severally liable for his own portion, and it is impossible to put any construction upon the words of the

> Act such as not to require the name of each of those persons to be specified, because undoubtedly the Arthur Average Association as an association in its joint capacity is not the underwriter, but each member, in proportion to the sum insured, becomes individually an underwriter. The Act, therefore requires his name to be mentioned in it, and if not, the policy is to be absolutely null and void. The names are not mentioned, and therefore the policy is absolutely null and void."

Counsel submitted that this case was clear authority for the proposition that something required to be specified in a document (in that case the insurance policy) must be contained within the document.

10 Counsel also referred to a passage in the Canadian case of *Re Paddle River Construction Company Limited* (1961) 35 WWR 605 where Greschuk J stated at 617 –

> ***"In my opinion, the clue to this whole matter depends upon the word "specified".*** Does this word mean that the contracts must be exactly named or specifically mentioned or particularized in the assignment before the assignment can come under subsec. (3)?
>
> ***In the New English Dictionary edited by Sir James Murray, LL.D., vol.*** 9, "specified" is defined as
>
> ***"that is or has been definitely or specifically mentioned, determined, fixed or settled."***
>
> ***The word "specified" as used in a similar section in England was discussed in*** *Re Cornish* , ***an unreported case which is considered in the following words in Williams on Bankruptcy, 17th ed., at pp. 354 and 355:***
>
> ***"The meaning, in the proviso, of the word 'specified' as applied to debtors and contracts was canvassed in*** *Re Cornish* , ***where the court would have felt happier with the word 'specific;' it was argued that it must mean that the debts are identifiable from some document recording the transaction, but this construction was rejected by the court, which assumed (without deciding) that the section applied to oral as well as to written assignments; in that case, the actual hiring agreements were handed over on the making of the advances charged thereon, and a receipt was given in which the reference numbers of the agreements were set out; these facts were held sufficiently to identify the agreements."***
>
> ***It would appear to me that having regard to the definition of the word "specified" and the manner in which it was dealt with in*** *Re Cornish* , ***that the words "specified contracts" do not means that the contracts are identifiable from some document recording the transaction.*** It seems to be that they must be unambiguously identified in the document itself."

Counsel for the plaintiff relied particularly on the last sentence of that extract.

11 Other statutory provisions which contained references to “specify” or “specified” were referred to by counsel for the defendant. In *Kaye v Croydon Tramways Company* [1898] 1 Ch 358 the English Court of Appeal considered the terms of section 71 of the Companies Clauses Consolidation Act 1845 which provided that “every notice of an extraordinary meeting…. shall specify the purpose for which the meeting is called”. Lord Lindley MR stated –

> ***“Now, what would anybody understand by that notice — anybody who was not behind the scenes, and did not know anything at all about the matter?*** He would understand from the notice that the meeting was convened for the purpose of considering a certain agreement for the sale of the undertaking and assets of the Croyden Tramways Company, and would assume as a matter of course that whatever the purchasing company was going to pay for the purchase of the undertaking and assets would be paid to the vendors — that is, would be paid to the selling company. That, however, is not true, because a very considerable portion of that which is part of the consideration for the purchase is not to be paid to the vendors, but is to be paid to the directors and officers of the selling company .
>
> ***Now comes the question – to my mind a difficult question – whether, in ordinary fairness of language, one can say that this notice does, to use the words of the Companies Clauses Act, “specify the purpose for which the meeting is called.”*** On behalf of the company it is argued that it does – that the purpose is to confirm the agreement. That, no doubt, is true by the card, but, in my opinion, this notice has been most artfully framed to mislead the shareholders. It is a tricky *370 notice, and it is to my mind playing with words to tell shareholders that they are convened for the purpose of considering a contract for the sale of their undertaking, and to conceal from them that a large portion of that purchase-money is not to be paid to the vendors who sell that undertaking. I am perfectly alive to the danger of putting into notices, especially notices by advertisement, more than the Act of the Parliament requires, and I agree that all that the Act of Parliament requires is that the purpose shall be stated. But it must be stated fairly: it must not be stated so as to mislead.”

12 Counsel for the defendant also referred to *Henderson v Bank of Australia* [1890] LR 45 Ch D 330 where Chitty J considered a notice that had to “specify the object for holding the meeting” and stated –

> ***“In cases of this kind it is settled that the notice which specifies the business to be done, or the objects of the meeting, is to be a fair notice, intelligible to the minds of ordinary men, the class of men who are shareholders in the company, and to whom it is addressed.*** The Court does not scrutinise these notices with a view to exercise criticism, or to find out defects, but it looks at them fairly. I think the question may be put in this form:

> What is the meaning which this notice would fairly carry to ordinary minds? That, I think, is a reasonable test. Another matter of very considerable importance in dealing with this as a practical question, is, how did the meeting itself understand the notice?"

Counsel for the plaintiff objected that these cases were not in point in that the matters required to be specified were in fact within the body of the relevant document (ie the notice) even if not adequately identified.

13 I return to these cases below, but for the present I observe that one conclusion to be drawn from them is that the meaning of "specify" is given colour by the context in which the word is used, and the purpose of the statutory provision in question.

14 The principal submission of counsel for the plaintiff, as stated above, was that the events of default must be contained within the body of the security agreement. His subsidiary submission, with which I deal first, was that **all** events of default must be contained within the agreement. Article 3(1)(f) referred to "events" in the plural. It followed, in counsel's submission, that if some events of default were specified in the security agreement but others were not, the statutory requirements were not fulfilled and the agreement was void. In my judgment, this submission is misconceived. The notion that the existence of one event of default, agreed between the parties but for some reason not embodied in the security agreement itself, could destroy the validity of an agreement which properly specified two other events of default, seems to me untenable. If an event of default is not specified in the agreement, then clearly no reliance may be placed upon it by the secured party. But the existence of an event of default which has either not been specified, or has been insufficiently specified in the security agreement, does not in my judgment, of itself, destroy the validity of a security agreement, provided that the agreement does adequately specify one or more other events of default.

15 Mr Robertson's principal submission was that the security agreement must contain within itself particulars of the events which are to constitute events of default. The security agreement should not incorporate other documents by reference. That would, in counsel's submission, give the same meaning to "specify" as to the phrase "contain provisions … sufficient to enable it to be identified". By the 1985 amendment to the Security Interests Law, the legislature had weakened the requirements in the other sub-paragraphs of Article 3(1) but had maintained a strict requirement that the events of default should be specified.

16 Counsel conceded that it was possible to identify the events of default in the EM TV security agreement, but only by following a paper chase through other agreements. "Event of default" was defined in the EM TV security agreement as meaning –

The "Financing Agreements" were defined in the recitals to the EM TV security agreement as meaning the Lehman Loan Agreement, the BLB Loan Agreement and the KM Loan Agreement, that is the agreements between, broadly, the Kirch Group and each of the lenders.

"Financing Documents" were defined as meaning "each and all of the Financing Agreements, the Security Documents and the Intercreditor Agreement".

"Intercreditor Agreement" was defined as meaning the agreement to which reference has been made in paragraph 2 above.

Thus, even at its simplest, it was necessary to refer to at least one external agreement in order to ascertain what an event of default was.

> *(a) in relation to the Financing Agreements an event of default howsoever described under any such Financing Agreement; or*
>
> *(b) a default by the Chargor in respect of its obligations to any of the Secured Creditors under any of the Financing Documents*.

17 Counsel submitted that this was not good enough. The security agreement should contain sufficient particulars both of the obligation which was secured and of the breach which would give rise to an event of default. These were significant matters which should be readily identifiable within the four corners of the security agreement.

18 Mr Thompson for the defendant stated that in the circumstances of this case his client was relying upon paragraph (b) of the definition of "event of default", that is "a default by the Chargor [ie the plaintiff] in respect of its obligations to any of the Secured Creditors under any of the Financing Documents". The plaintiff had guaranteed the obligations of FEB, which had defaulted. It was the breach of that obligation which was at the heart of the matter. All the phrases in paragraph (b) were defined in the EM TV security agreement. It was only necessary to go outside the security agreement when looking at the definition of Financing Documents, which contained a reference to 'Security Documents'. But the agreement specifically incorporated the definitions in the Intercreditor Agreement. Clause 1.1 of EM TV security agreement provided –

> *In this Security Agreement unless the context otherwise requires or unless otherwise defined or provided for herein, words and expressions shall have the same meaning as is attributed to them under the Intercreditor Agreement (as defined below).*

The Intercreditor Agreement contained a definition of Security Documents. That definition included a reference to secured assets, which included the issued share capital of Speed, which took one straight back to the EM TV security agreement.

19 Counsel accordingly submitted that particulars of the secured obligation and of the breach leading to an event of default were all to be found in the EM TV security agreement. It was perfectly permissible to incorporate documents by reference. The EM TV security agreement specifically incorporated definitions contained in the Intercreditor Agreement. Counsel contended that the principle of incorporation by reference was particularly

sensible in the context of security agreements as part of complex financing arrangements in order to avoid unnecessary repetition and cumbersome documentation. He referred to a passage from a judgment of Oliver LJ in *Skips Nordhiem v Syrian Petroleum* [1984] QB 599 at 619 where the learned Lord Justice stated –

> ***"The purpose of the referential incorporation is not – or at least is not generally – to incorporate the intentions of the parties to the contract whose clauses are incorporated but to incorporate the clauses themselves in order to avoid the necessity of writing them out verbatim.*** The meaning and effect of the incorporated clauses has to be determined as a matter of construction of the contract into which it is incorporated having regard to all the terms of that contract."

20 Counsel for the defendant placed some reliance on article 3(2) of the Security Interests Law which provides that a security agreement may "contain **or refer"** [my emphasis] to such matters as may be agreed between the parties. While this may be indicative of an intention on the part of the legislature to create some flexibility in the manner in which the parties can express their agreement, it does not assist to counter the argument of the plaintiff. Paragraph (2) is subject to paragraph (1). If therefore paragraph (1) requires that all particulars of events of default should be contained within the security agreement, paragraph (2) does not avail.

21 Article 3(1)(f) of the Security Interests Law provides that the security agreement shall "specify the events which are to constitute events of default". I take the words "name (something) definitely or explicitly" in the definition of "specify" in the Oxford English Dictionary as being most apt to this particular context. In my judgment the essence of the requirement is that there should be an absence of ambiguity. The events of default should be definitely or explicitly set out. There should not be any doubt as to what the events of default are. Plainly this is very important, because if an event of default occurs steps may be taken to enforce the security.

22 In the company convening notice cases referred to by Mr Thompson "specify" was held to require that the object of the meeting be stated fairly and clearly. In the Paddle River case there was a general statutory provision that the assignment of book debts should be void against a trustee in bankruptcy. A saving provision exempted debts "under specified contracts". One can understand why the court in that case should have adopted a narrow construction and held that such contracts should be "unambiguously identified in the document itself". In this context, however, I reject the submission that "specify" requires all the particulars of the events of default to be contained within the security agreement itself. Such a construction would impose a straitjacket that is not required by the words of the statute. If the legislature had intended that the particulars of the events of default should be contained within the security agreement itself, express provision could easily have been made to that effect. No such provision was made, and indeed in other parts of the Security Interests Law (article 3(2) for example) there is evidence that the legislature intended a measure of flexibility as to the manner in which parties could express their agreement. The

legislature did not proscribe the incorporation by reference of particulars of the events of default. To construe the statute in that way would not only run counter to the presumed intention of the legislature, but would also produce inconvenience in that security agreements would become longer and more complex. Provided that the events of default can be definitely or explicitly identified in the security agreement and any documents incorporated by reference, the requirements of article 3(1)(f) of the Security Interests Law are in my judgment satisfied. Clearly, the longer the paper-trail, and the more convoluted the cross-referencing may be, the greater the scope for argument that ambiguities exist. In the context of the EM TV security agreement there is, in my judgment, no ambiguity. The event of default specified at paragraph (b) of the definition in the security agreement is explicitly set out and I accordingly find that the agreement is valid and effective.