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Kirkland Alert

2021 in Review: Key UK Commercial Cases

11 January 2022

As 2022 gets under way, and we are once again in the throes of a COVID-19 wave, it may seem that we are no further forward than 2020. However, 2021 featured a number of important decisions, not least those with their roots in the unique sets of challenges that the pandemic has thrown up for insurance companies and other commercial parties. We look back at the most notable commercial cases decided by the English courts (and Privy Council) over the course of 2021.

Business Interruption Insurance — FCA Test Case

2021 started out with the UK Supreme Court handing down its decision in the business interruption ("BI") insurance test case brought by the Financial Conduct Authority (the "FCA") with respect to losses caused by COVID-19 (the "Test Case").[1] This is a major decision, which the Supreme Court estimates will affect some 370,000 policyholders.

The FCA sought to clarify coverage issues in sample BI insurance policies covering losses caused by: (i) infectious or notifiable diseases ("disease clause"); or (ii) prevention of access and public authority closures/restrictions ("prevention of access and hybrid clause") (these are clauses that covered more than business interruption caused by physical damage to property).

The FCA selected 21 examples of policy language issued by eight insurers for the Test Case. The High Court found that most of the disease clauses and some of the prevention of access clauses provided cover for BI losses caused by COVID-19.

The Test Case was leap-frogged to the Supreme Court which, in January 2021, found largely in favour of the insureds, ruling that most of the policies on appeal (some were not appealed) provided cover for BI losses caused by COVID-19 where such policies contained a disease or prevention of access and hybrid clause.

Disease Clauses

The Supreme Court held that disease clauses would cover BI losses where the proximate cause was cases of COVID-19 that occurred within the specified radius of the insured premises. The Supreme Court found that causation could be proved by showing that the interruption was a result of government action taken in response to at least one case of COVID-19 within the relevant geographical area. Each individual case of COVID-19 that had occurred by the date of any government action was a separate and effective cause of that action (and of the response of the public to it).

Prevention of Access and Hybrid Clauses

The Supreme Court held that prevention of access and hybrid clauses covered BI losses that resulted from all of the elements of the insured peril acting in combination to cause BI loss. Such a loss would be covered regardless of whether the loss was concurrently caused by other (uninsured but non-excluded) consequences of the COVID-19 pandemic, provided that the concurrent causes were of approximately equal efficacy. Thus, if it was found that, while all the elements of the insured peril were present, the peril itself could not be regarded as a proximate cause of the loss, then the loss would not be covered. The Supreme Court gave the example of a travel agency that lost almost all its business because of the COVID-19 travel restrictions. Whilst customer access to its premises might have become impossible, if the sole proximate cause of the loss of the agency's walk-in customer business was restrictions on foreign travel, and not the inability of customers to enter the agency, then the loss would not be covered.

Trends Clauses

The usual function of a 'trends clause' is to regulate the quantum of the insured loss to ensure that it is not inflated by uninsured reasons. In this case, the Supreme Court considered whether trends clauses put before it entitled insurers to reduce their indemnity to account for the fact that, even if the insured had remained open for business, it would still have suffered interruption loss because of the effects of the COVID-19 pandemic.

The Supreme Court noted that "*the aim of such clauses is to arrive at the results that would have been achieved but for the insured peril and circumstances arising out of the same underlying or originating cause*".[2] The Supreme Court emphasised three points with respect to trends clauses: (i) they are part of the machinery for quantifying loss. They do not address or seek to delineate the scope of the indemnity (which is the function of the insuring clauses); (ii) they should, if possible, be construed consistently with the insuring clauses; and (iii) "*if possible, they should be construed so as not to take away the cover provided by the insuring clauses. To do so would effectively transform quantification machinery into a form of exclusion.*"[3]

The Supreme Court has issued a set of declarations which apply to the policies that were in consideration in the Test Case and note whether those policies provide cover. The decision is very complicated and to some degree specific to the policy language being considered (bearing in mind that the purpose of the Test Case was to give general guidance). In addition, those parts of the original High Court judgment that were not appealed still stand. Specific BI policy language should be considered in light of both decisions.

Supreme Court expands Parent Company liability for acts of subsidiary

The Supreme Court's decision in *Okpabi v Royal Dutch Shell Plc* [2021] UKSC 3 is notable as it considered the circumstances in which a UK-domiciled parent company may owe a common law duty of care to individuals for the actions taken by its foreign subsidiary.

The claim was brought by individuals in Nigeria seeking compensation in relation to environmental damage, which resulted from oil spills in Nigeria caused by the alleged negligence of the operator of the relevant pipeline. The operator, The Shell Development Company of Nigeria ("SPDC") is a Nigerian-registered company and a subsidiary of Royal Dutch Shell PLC ("RDS"), a company incorporated in the UK.

The claimants sought permission to serve proceedings outside the jurisdiction on SPDC on the ground that it was a "*necessary or proper party*" to the claims against RDS for the purposes of the jurisdictional "gateway" in paragraph 3.1(3) of Practice Direction 6B of the Civil Procedure Rules. In order for jurisdiction against SPDC to be established under this gateway, the claimants needed to establish that their claims against RDS, as the anchor defendant, raise a real issue to be tried — i.e., that they have a real prospect of success.[4]

The claimants argued that RDS owed them a common law duty of care because it exercised significant control over material aspects of and/or assumed responsibility for, SPDC's operations, including by promulgating and imposing mandatory health, safety and environmental policies.

The claimants relied on the Supreme Court's decision in *Vedanta Resources Plc v Lungowe* [2019] UKSC 20, which confirmed that parent company liability is to be considered on ordinary tort principles regarding the imposition of a duty of care. Whether a duty of care arises will depend on the extent to which the parent took over, intervened in, controlled, supervised and/or advised the management of the subsidiary's relevant operations.

In *Okpabi*, the Supreme Court unanimously held that there was a serious issue to be tried as to whether a duty of care arose as a result of RDS' management or joint management of SPDC's activities and the promulgation by RDS of group-wide safety and environmental policies as well as taking active steps to ensure their implementation by SPDC. The Supreme Court adopted the analysis of Sales LJ in the Court of Appeal[5] in which he considered the vertical organisation of the Shell group, along business and functional lines, to be significant despite the parties' separate corporate status.

The decision in *Okpabi* considered only whether there was a serious issue to be tried; it did not consider the merits of the duty of care claim. It is, however, significant, as *Okpabi* along with *Vedanta* has confirmed that in the right circumstances a parent company may be liable in tort for the actions of its subsidiary. The parent company cannot rely on a defence of corporate structure alone.

When can a party set aside a contract on the grounds of "lawful act economic duress"?

Pakistan International Airline Corporation v Times Travel (UK) Ltd [2021] UKSC 40 considered whether a party can set aside a contract on the ground that it was entered into as a result of the other party threatening to cause economic harm through a lawful act — so called 'lawful act economic duress'.

Times Travel ("TT") is a travel agent that almost exclusively sold flight tickets to Pakistan operated by Pakistan International Airline Corporation ("PIAC"). PIAC was entitled to terminate this arrangement on one month's notice.

A dispute arose between PIAC and its travel agents, including TT, over allegations of unpaid commissions. TT did not join claims to recover unpaid commissions due to pressure from PIAC. PIAC subsequently reduced TT's ticket allocation by 80% and gave notice that it would terminate their arrangement in one month. TT agreed to new terms with PIAC during the one-month notice period, including waiving claims for unpaid commissions (the "New Agreement"). TT subsequently brought a claim against PIAC for the unpaid commission, arguing that it could rescind the New Agreement for lawful act economic duress.

The question before the Supreme Court was whether the actions of PIAC constituted an illegitimate threat. The Supreme Court found that the doctrine of lawful act economic duress does exist as a matter of English law and that it has three necessary elements: (i) the threat or pressure must have been illegitimate; (ii) the threat or pressure must have caused the claimant to enter the contract; and (iii) the claimant must have had no reasonable alternative to giving in to the threat or pressure. If all three can be shown, the court may rescind a contract entered into as a result of the duress.

The Supreme Court noted that it will be rare for a court to find lawful act economic duress in respect of negotiations between commercial parties. The Supreme Court noted that there are only two circumstances in which lawful act economic duress has been recognised: (i) where knowledge of a person's criminal activity is used to threaten them; and (ii) where a defendant uses reprehensible means to manoeuvre a claimant into a position of vulnerability to force it to waive its claim. In both circumstances, the courts have been influenced by equity.

On the facts of this case, the majority held that PIAC giving notice to terminate the contract and reducing TT's ticket allocation was not reprehensible conduct. In addition, PIAC's genuine belief that it was not liable to pay the disputed commission further supported the view that its behaviour was not reprehensible.

This case shows that the doctrine of lawful act economic duress exists in English law, that its application is narrow and courts will rarely make such a finding in a commercial context.

Governing law of an arbitration agreement

2021 saw another Supreme Court decision on the governing law of an arbitration agreement, following last year's decision in *Enka*.[6]

Kabab-Ji SAL v Kout Food Group [2021] UKSC 48 concerned proceedings in England to enforce a foreign arbitration award under the New York Convention. Arbitration proceedings were brought pursuant to an arbitration agreement contained in a franchise agreement between Kabab-Ji and Al Homaizi Foodstuff Company ("AHFC"). Following a corporate reorganisation, AHFC became a subsidiary of Kout Food Group ("KF").

When a dispute arose under the franchise agreement, Kabab-Ji commenced arbitration in Paris against KF, not AHFC. The tribunal found that KF was a party to the franchise agreement and the arbitration agreement contained therein and that it had breached the franchise agreement. Kabab-Ji sought to enforce the award against KF in England. KF opposed the enforcement of the award on the basis that the arbitration agreement was invalid.

Three issues were before the Supreme Court, one of which was a determination of which law governed the validity of the arbitration agreement. The Supreme Court refused to enforce the award on the basis that English law applied to the arbitration agreement and, that accordingly, under English law KF had not become a party to the arbitration agreement.

In determining the governing law of the arbitration agreement, the Supreme Court noted that in the absence of an international consensus between national courts as to the meaning of the conflict of laws rules in the New York Convention, the English court would need to form its own view based on first principles. Taking into account these first principles (which included those set out by the Supreme Court in its 2020 decision in *Enka*), the Supreme Court held that a general choice of law clause in a contract containing an arbitration agreement was a sufficient indication that the parties had intended English law to apply to the arbitration agreement — particularly where the governing law clause applied to the whole agreement. This was true, even where the arbitration was seated in a different jurisdiction (in this case, Paris).

This decision builds upon and confirms the Supreme Court's judgment in *Enka*, providing welcome clarity and certainty as to how the English courts will approach determining the governing law of an arbitration agreement.

Pre-arbitral steps are not matters of jurisdiction

The English court confirmed in two cases that, contrary to indications in some earlier decisions, an arbitral tribunal will have jurisdiction to consider a dispute even where contractual pre-arbitral steps have not been taken.[7]

In both cases, the defendants to the arbitration challenged the award in the English courts under section 67 of the Arbitration Act 1996 on the basis that the tribunals did not have jurisdiction to hear the claims because pre-arbitral steps in the relevant multi-tiered dispute resolution clauses had not been followed. The key distinction was between whether a failure to follow pre-arbitral steps went to: (i) the admissibility of the claim (i.e., whether the tribunal should consider the claim — an issue to be determined by the tribunal); or (ii) the jurisdiction of the tribunal to consider the claim at all.

In *Republic of Sierra Leone v SL Mining Ltd*, the court noted that the key issue was whether the alleged prematurity in bringing arbitration proceedings meant that the dispute had not been submitted to arbitration in accordance with the arbitration agreement. The court concluded that where the issue relates to whether a claim has been brought too early, the issue is of admissibility and is one best decided by the tribunal.

In *NWA & FSA v NVF & others*, the court added that it was not appropriate to interpret pre-arbitral *procedural* requirements as jurisdictional issues since non-compliance did not affect whether the dispute was the kind of dispute that the parties had agreed to submit to arbitration. The judge noted that treating these steps as a condition precedent would lead to the absurd result that if one party refused to mediate, the tribunal would never gain jurisdiction over the dispute, which cannot have been the parties' intention.

High Court gives guidance on internally inconsistent dispute resolution clauses

Melford Capital Partners (Holdings) LLP v Frederick Digby illustrates that when presented with a contract containing two seemingly opposed forms of dispute resolution, the English courts will take a pragmatic and pro-arbitration approach.

Melford concerned a complex partnership dispute centred on two agreements, including a limited liability partnership agreement (the "LLP Agreement") which was governed by English law and contained both an arbitration clause and an exclusive jurisdiction clause in favour of the English courts ("EJC").

Melford commenced proceedings in the English courts against Digby. When serving his defence, Digby made a counterclaim against Melford. Melford later commenced arbitration proceedings against Digby pursuant to the LLP Agreement and subsequently applied to the English court to stay Digby's counterclaim. Digby argued that the arbitration clause was of no effect as it was irreconcilable with the EJC.

The court recognised that these were sophisticated parties who would have gone to some trouble to negotiate an agreement that their disputes would be resolved through arbitration. The court was unwilling to accept that the arbitration clause was a provision that could be cast aside so easily. The court therefore concluded that the arbitration clause was a valid and separable agreement, with the EJC being limited to the English court retaining supervisory jurisdiction over the arbitration.

This is a robust, pro-arbitration decision and a clear demonstration of the confusion that can arise from improperly drafted dispute resolution clauses.

Stricter rules for witness statements in England & Wales came into force

In April 2021, a new practice direction on trial witness statements came into force. PD 57AC applies to all trial witness statements in the Business & Property Courts of England and Wales (save for a few exceptions) signed on or after 6 April 2021. PD 57AC has not changed the law on witness evidence.[8] Rather it seeks to change the practice by which trial witness statement are produced by, for example, requiring witnesses and legal representatives to provide confirmations and certifications of compliance with PD 57AC.

PD 57AC also seeks to produce change by imposing a stricter approach to witness statements which fail to comply with the rules on witness evidence. The court has also been given the ultimate sanction of striking out non-compliant witness statements. While in the nine-plus months since the introduction of PD 57AC, the court has not yet struck out a whole witness statement for non-compliance, the courts have been willing to strike out portions of a witness statement. For example, in *Mansion Place Ltd v Fox Industrial Services Ltd* [2021] EWHC 2747 (TCC), the court struck out parts of witness statements that merely commented on documents or contained impermissible argument while in *Blue Manchester Ltd v Bug-Alu Technic GmbH* [2021] EWHC 3095 (TCC), the court ordered the defendant to re-draft those parts of the witness statement that did not comply with PD 57AC. The court usefully set out in an appendix to the judgment why the offending parts of the witness statement did not comply with the rules and the changes that were required.

Thus far, the courts have taken a firm but fair approach to the application of PD 57AC. While judges have taken a more interventionist approach as parties and their legal advisors adjust to the new rules, the courts have made clear that they expect parties to first seek to resolve any disputes between themselves. As the judge in *Blue Manchester* warned, those who indulge in unnecessary trench warfare will be penalised in costs.

No such thing as “temporary frustration”

There have been a number of commercial rent arrears cases working their way through the courts in 2021, as landlords seek payment of rents that have accrued since March 2020. In *Bank of New York Mellon (International) Ltd v Cine-UK Ltd* [2021] EWHC 1013 (QB), one argument put forward by the tenants in defence of the summary judgment claim was that they were relieved from their payment obligations due to a suspensory frustration — i.e., a short-term frustration following which the leases would continue as before.

The court rejected this contention (and all of the other tenants’ arguments) and granted summary judgment in favour of the landlord. The court found that English law does not recognise “temporary frustration” and the argument had no real prospect of success. The court noted that an act of frustration does not suspend the contract and that the effect of frustration is that it brings the contract to an end (and so cannot be temporary). For a contract to be frustrated there must have been a "radical" change in circumstance, which renders it unjust for the contract to continue. Where such a "radical difference" does not exist, there cannot be frustration. We understand that Cine-UK Ltd has been granted permission to appeal to the Court of Appeal.

Privy Council further narrows rule against claims for 'reflective loss'

Investors seeking to recover their losses through litigation often come up against the 'rule against reflective loss', which prevents a shareholder from bringing a claim in respect of a diminution in the value of its shareholding or reduction in the distributions which it receives, where those reflect a loss suffered by the company in which it is invested. The force of this principle was significantly lessened by the UK Supreme Court's 2020 decision in *Marex Financial Ltd v Sevilleja* [2020] UKSC 31, which narrowed the principle to a bright line rule limited to shareholders who claim for the loss in the value of their shares or distributions, where that loss is a consequence of the company having suffered loss, in relation to which the company has a cause of action.

The issue in *Primeo Fund v Bank of Bermuda (Cayman) Ltd* [2021] UKPC 2 was whether the reflective loss rule barred a fund ("Primeo") which had purchased shares in a fund which was part of Bernie Madoff's Ponzi scheme ("BLMIS") which, as a result of the fraud, were worth far less than their acquisition price. Primeo's BLMIS shares were later transferred to another fund ("Herald") such that Primeo ceased to directly hold its interest in BLMIS (and was instead an indirect holder through Herald). This transfer occurred prior to this litigation being commenced.

The Board held that the reflective loss rule did not bar Primeo from claiming in respect of the losses it suffered each time it made a direct investment in BLMIS (i.e., the loss from it having paid significantly more for the shares than they were worth), nor from claiming in respect of the loss of the chance to redeem those investments prior to Primeo transferring its BLMIS interest to Herald. Those losses were not suffered by Primeo "*in its capacity as shareholder*" of Herald since at the time Primeo suffered such losses it was not a shareholder in Herald and was therefore not barred by the rule against reflective loss. This is an important further narrowing of the rule against reflective loss.

Court of Appeal clarifies “reasonable detail” requirement in an SPA Breach Notice

Businesses are typically sold through a SPA containing a host of warranties, indemnities and covenants by which the seller promises to make the purchaser whole for specified losses. SPAs typically provide an internal code for how and when claims may be made. Buyers are typically required to notify sellers in writing of any claim before a specified deadline, specifying in reasonable detail the matter which gave rise to the claim, the nature of the claim and the amount claimed. SPAs do not typically specify what amounts to ‘reasonable detail’, and it is not uncommon for buyers and sellers to end up in a dispute over whether a notice conformed to the requirements of the SPA, particularly where the claim would otherwise be out of time.

Dodika Ltd v United Luck Group Holdings Ltd [2021] EWCA Civ 638 was such a case. Shortly before the deadline for claims expired, the buyer notified the sellers of a claim under a tax covenant. The notice explained that the claim related to an investigation by a tax authority and set out a brief chronology. As the investigation was ongoing, the buyer was not able to quantify its claim. The sellers rejected the notice and the buyer brought proceedings.

The High Court held that while it was not necessary to quantify the claim as it was not yet possible to do so, the mere reference to an investigation by a tax authority into transfer-pricing activities did not provide sufficient information of the matter giving rise to the claim and the notice was therefore invalid.

The Court of Appeal disagreed. The judges concluded that the matter giving rise to the claim was the target group’s transfer-pricing practice, rather than the mere fact of a tax investigation. However, they held that the notice provided reasonable detail of the issues arising out of that practice for the purposes of the SPA for three primary reasons:

1. The sellers were aware of the detail of the tax authority’s investigation and the notice had to be read in that context.

2. There was very little specific detail available to the buyer and any further detail would only have been high level.
3. The notice had to be considered in light of the commercial purpose of the requirement for "reasonable detail", which was to enable sellers to make enquiries into the factual circumstances of a claim so as to assess its merits. It served no commercial purpose to set out further "*limited and generic detail*" or to recite facts which the sellers already knew.

Thus when sending a notice of breach, parties should take care to provide as much detail as possible. However, in so doing they are entitled to bear in mind the reality of the situation, including the facts already known to the other party and the information actually available to them.

Post-Brexit Developments

Finally, no disputes review would be complete without a mention of Brexit. The European Commission dealt a blow to the hopes of the UK's accession to the Lugano Convention when, in May 2021, it recommended that the EU should not consent to the UK's accession and, in June 2021, deposited a *Note Verbale* with the Swiss Federal Council as Depositary of the Lugano Convention that the EU was not in a position to consent to the UK's accession. The European Commission's position being that the Lugano Convention is a "*flanking measure*" of the EU's internal market and for its relations with the European Free Trade Association[9] countries. The European Commission maintains that multilateral conventions such as the Convention of 30 June 2005 on Choice of Court Agreements (i.e. the Hague Convention on Choice of Court Agreements) provide the relevant framework between the UK (as a third country) and the EU for matters of civil jurisdiction and the enforcement of judgments.

In 2021, the English courts also heard a number of cases dealing with a variety of legal consequences arising out of the UK's departure from the EU and the end of the transition period. We do not propose to go into each of these cases since they alone could be the subject of an annual review. However, it has been encouraging to see that the English courts have thus far taken a pragmatic approach to the interpretation and application of retained EU law and principles, even where they have had the opportunity to depart from them.

Conclusion

As is apparent from this *Alert*, 2021 was a big year for commercial litigants and the courts, which, undeterred by the ongoing pandemic, litigated major cases leading to important decisions.

If you would like to discuss any of the cases in this *Alert*, please do not hesitate to reach out to the authors or your usual Kirkland contact.

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1. *The Financial Conduct Authority & Ors v Arch Insurance (UK) Ltd & Ors* [2021] UKSC 1.↩

2. *The Financial Conduct Authority & Ors v Arch Insurance (UK) Ltd & Ors* [2021] UKSC 1 [268].↩

3. *The Financial Conduct Authority & Ors v Arch Insurance (UK) Ltd & Ors* [2021] UKSC 1 [262].↩

4. See *Altimo Holdings and Investment Ltd v Kyrgyz Mobil Tel Ltd* [2012] 1 WLR 1804 [82]; *Vedanta Resources Plc and another v Lungowe and others* [2019] UKSC 20 [42].↩

5. *Okpabi and others v Royal Dutch Shell Plc and another* [2018] EWCA Civ 191.↩

6. *Enka Insaat Ve Sanayi AS v OOO "Insurance Company Chubb"* [2020] USKC 38.↩

7. *Republic of Sierra Leone v. SL Mining Ltd* [2021] EWHC 286 (Comm) and *NWA & FSA v NVF & others* [2021] EWHC 2666 (Comm)↩

8. As has been confirmed in, for example, *Mad Atelier International BV v Manes* [2021] EWHC 1899 (Comm) and *Mansion Place Ltd v Fox Industrial Services Ltd* [2021] EWHC 2747 (TCC).↩

9. The European Free Trade Association countries that are signatories to the Lugano Convention are: Switzerland, Norway and Iceland.↩

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Suggested Reading

- 11 January 2022 Kirkland Alert 2022 EU Antitrust & FDI Update
- 11 January 2022 Press Release Kirkland Adds IP Litigation Partner Kat Li
- 04 January 2022 Award D Magazine Best Lawyers Under 40 2022