
FORTIFICATION OF CROSS- UNDERTAKINGS

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Introduction

- Why apply for fortification of a cross-undertaking?
- Until recently, a number of broadly equivalent tests applied by first instance judges, with no judicial treatment at the appellate level.
- Recent decision of the Court of Appeal in Energy Venture Partners Limited v Malabu Oil and Gas Limited [2014] EWCA Civ 1295:
 - Affirms the approach taken by most first instance judges; and
 - Consolidates the previous authorities into a three-fold test



The Facts in Energy Venture

- The Appellant, EVP, secured a worldwide freezing injunction against the Defendant, Malabu. Malabu subsequently paid US\$ 215 million into court following an arrangement between the parties.
- Prior to Malabu's payment into court, the Appellant was required to fortify its cross-undertaking by means of a written guarantee in the sum of US\$ 150,000.
- Following its payment into court, Malabu applied for further fortification to reflect the losses arising from having US\$ 215 million blocked in a bank account attracting 0.15% interest *per annum*.
- Hamblen J granted fortification for £10 million.



The Test Applied by the CA

- Based principally on the decisions of Briggs J (as he then was) in Harley Street Capital [2005] EWHC 2471 (Ch) and Jirehouse Capital [2008] EWHC 725 (Ch), and of Mann J in Sinclair Investment [2004] EWHC 218 (Ch).
- A three fold test (at [53]):
 - *“Broadly speaking, they require an intelligent estimate to be made of the likely amount of any loss which may be suffered by the applicant for fortification (here the defendants) by reason of the making of an interim order.”*
 - *“They require the court to ascertain whether there is a sufficient level of risk of loss to require fortification.”*
 - *“They require that the loss has been or is likely to be caused by the granting of the injunction.”*



The Burden of Proof

- The applicant must show a good arguable case for each limb of the test.
- Tomlinson LJ endorsed the principle of “*symmetry*” set adopted by the first instance judge (Hamblen J).
- At [52]: “*Since the Claimant has obtained a Freezing Order preserving assets over which it may be able to enforce on the basis of having shown the court that it has a good arguable case, it is only appropriate that if the Defendant can show that it too has a good arguable case that it will suffer loss in consequence of the making of the order, it should equally be protected*”.



(1) An Intelligent Estimate of Loss

- At [53]: “*In some cases the assessment of loss may at the interlocutory stage be difficult. It is in such cases that an intelligent estimate is required. An intelligent estimate will be informed and realistic although it may not be entirely scientific*”.
- On the facts of the case, Tomlinson LJ concluded that it was reasonable, at an interlocutory stage, to assume that “*the prima facie effect of the Freezing Order*” was that in order to meet a liability from funds paid in court, a party would need to borrow the same amount of funds. The “*intelligent estimate*” of loss, in these circumstances, is an interest claim based on the cost of borrowing (at [57]).



(2) Sufficient Risk of Loss

- To show a sufficient risk of loss is “*synonymous with showing a good arguable case to that effect*” (at [53]). Or, as put by Hamblen J: “*The position is that the claimant has security for its claim on the basis of having shown the court that it has a good arguable case. If, as I find to be the position, the defendant can show that it too has a good arguable case that it will suffer an interest loss if it succeeds in this action and enforces the cross-undertaking, then it should equally be protected*” (cited at [22]).
- The financial position of the applicant is irrelevant in assessing its risk of loss. At [20], Hamblen J: “*It was not correct to suggest that a rich claimant could not recover interest for loss of the use of his money*”.

(3) A Causal Link

- The interim order which has been the subject of the cross-undertaking must be a *but for* cause of the alleged loss.
- At [54]: “*At the stage of considering whether fortification of the undertaking is required, the proposition could be restated as it is sufficient for the court to be satisfied that the making of the order is or was a cause without which the relevant loss would not be or would not have been suffered*”.
- Tomlinson LJ explained that it was open to the Respondent to challenge the causal link, but that if “*disproving the asserted causal link as to which a good arguable case is shown requires the deployment of extensive contentious evidence and argument, that is not an exercise to be attempted at the interlocutory stage*”.

The Decision in Energy Venture

- First instance decision granting fortification upheld.
- There was insufficient evidence to support the view that Malabu was ‘a corrupt moneybox’, used to funnel corrupt funds (at [56]).
- It is irrelevant, at the interlocutory stage, whether Malabu would in fact have borrowed funds to cover its liabilities relating to the funds paid in court. The *prima facie* position is that funds paid in court will not be available, and that is sufficient to satisfy the burden of proof at the interlocutory stage (at [57]).
- There was insufficient evidence to displace the presumption that the cost of borrowing is the appropriate measure of loss (at [58]).



The Old Law Remains Good Law

- The CA restated the position under the existing case law, which remains good law, and it provides some helpful input in applying the test.
- For example:
 - Bloomsbury International Limited [2010] EWHC 1150 (Ch): the balance of convenience might be relevant. “*In a case where one finds, as I have, that a defendant is at risk of significant harm if it turns out that a freezing order has been wrongly granted, it is material to enquire whether there is any corresponding harm to the claimant if fortification is ordered*” (at [29]).



The Old Law (cont)

- More examples:
 - Sinclair Investments [2004] EWHC 218 (Ch): the strength of the parties' case on the merits is neither a relevant nor an appropriate consideration during an application for fortification (at [18]).
 - Harley Street Capital: the applicant must show that it is the interim order that is causing the loss, rather than the substantive proceedings themselves. E.g. is the drop in the value of shares caused by a freezing order, or because the shares are the subject of a major litigation? (at [35])



Factual Matrices from Jurisprudence

- Sinclair: the applicant argued that he intended to use his frozen property as security for a business, and that he suffered loss as a consequence. The judge declined to order fortification as the applicant had not shown that he could not have used a non-frozen asset as security.
- Harley Street Capital: the applicant argued that the frozen shares had fallen in value. The judge declined to order fortification as the evidence of a causal link was too weak.
- Jirehouse: the applicant argued that it would suffer £150,000 loss, but the judge’s “intelligent estimate” was a loss of £15,000. The judge declined to order fortification as the respondent could pay £15,000.



Factual Matrices (cont)

- Bloomsbury international: fortification sought against insolvent companies in administration, in the light of a £210 million freezing injunction secured by the companies. Fortification granted to the sum of £4 million, principally on a balance of convenience analysis (at [29] and [30]).
- Fortress Value [2012] EWHC 1486 (Comm): increased fortification sought (from EUR 4 million to EUR 25 million) in the light of a freezing order against an entire investment structure. The alleged loss is that no further investors will be willing to invest in the structure. Judge refused to grant fortification, on the basis that the grounds for applying were speculative, and unsupported by probative evidence.



Practical implications

- Although not a mini-trial, it is essential to present the judge with clear evidence of a potential loss:
 - Where funds are paid in court (e.g. for security for costs), this will be relatively straightforward.
 - Where assets are simply frozen (e.g. property or shares), the evidence will need to be far more compelling.
- Causation: need to show the freezing injunction is a but for cause of loss.
- A related issue – how to quantify the loss suffered once the cross-indemnity, fortified or otherwise, is called upon. A recent Court of Appeal decision in Richard John Hone [2014] EWCA Civ 711 deals with this separate point.

