COMFORT LETTER BINDS TIN COMPANY

KLEINWORT BENSON LTD vs MALAYSIAN MINING CORPORATION BERHAD
Queen's Bench Division (Commercial Court): Mr Justice Hirst, December 21st,.1987

LETTER of comfort forming an important and integra1 part of a commercial agreement made for consideration, has contractual status if its wording is apt to create a contract, and if the importer fails to prove a common intention that it could not be legally binding.

Justice Hirst so held in giving judgment for the plaintiff, Kleinwort Benson on its claim against Malaysian Mining Corporation Berhad under a letter of comfort furnished by Malaysian to :Kleinwort in support of a loan toMalaysian's subsidiary, MMC Metals Ltd.

His lordship said that in 1983 Malaysian Mining formed MMC Metals as a wholly-owned subsidiary, to operate as a dealing member of the London Metal Exchange.

Metals required substantial extra funding. There were discussions between Malaysian and Kleinwort. Kleinwort. offered Metals a facility of £5m on terms that Metals and Malaysian should be jointly and severally liable. It proposed that Malaysian should guarantee the loan.

Malaysian said its policy was not to guarantee its subsidiaries' borrowing. Kleinwort therefore proposed that it would furnish a letter of comfort.

Malaysian's directors decided by formal resolution that Metals should be authorized to accept the facility, and that a letter of comfort should be issued to Kleinwort.

The letter of comfort referred to the £5m facility and stated:

> *(1) "We hereby confirm that we know and approve of these facilities and are aware…they have been granted...because we control MMC Metals."*
>
> *(2) "We confirm that we will not reduce our current financial interest in MMC Metals until the above facilities have been repaid."*

The crucial paragraph was paragraph (3).

It stated:

> *"It is our policy to ensure that the business of MMC Metals is at all times in a position to meet its liabilities to you under the above arrangements."*

Early in 1985 the facility was increased to £10m. On the collapse of the tin market in October 1985 Metals ceased trading, and on November 11 Kleinwort terminated the facility. By that time the full £10m had been drawn.

Kleinwort demanded immediate payment. It was not forthcoming. Shortly afterwards Metals went into liquidation. Malaysian renounced liability. It said the statements in the comfort letter were not intended to and did not impose any legally binding obligation to support Metals.

The main question for the court was whether the crucial paragraph was contractual in status.

The general principle was that an agreement, though supported by consideration, was not binding as a contract if made without any intention creating legal relations (see *Chitty on Contracts 25th ed para 123).*

In *Edwards vs Skyway*: [1964] WLR 349 Mr Justice Megaw said there were cases where an agreement did not give rise to legal rights because the parties had not intended that their legal relations should be affected. But, he said, where. the agreement related to business affairs, not social or domestic matters, the onus of proving there was no such intention was on the party who asserted that no legal effect was intended, and the. onus was heavy.

In *Chemco Leasing*, unreported July 19 1985 (upheld in the Court of Appeal [1987] FTLR 201), Mr Justice Staughton said with regard to letters of comfort, that when businessmen wished to conclude a bargain but could not agree on some particular aspect, it was not uncommon for them to adopt language of deliberate equivocation so that the contract might, be signed and their main objective achieved.

In reality, he said, the common intention was that, if all did not go well, the terms should mean what the court or arbitrator decided they meant - 'Nevertheless, I must carry out the traditional task of ascertaining what common intentions should be ascribed to the parties from the terms of the ...documents in question and the surrounding circumstances.'

The present court had to carry out the same traditional

task, having regard to the proper construction of the written words in their surrounding circumstances, and without regard to evidence from the parties or anyone else as to what they thought the contract meant or was intended to mean. Extrinsic evidence might however he admissible to show that what appeared to be a valid and binding contract was in fact no contract at all *(see Chitty, para 805).*

Mr Waller for Kleinwort relied on *Edwards v Skyways*. He 'submitted there was a heavy onus on Malaysian to prove there was no intention to create contractual relations. He said all the circumstances pointed to the contrary.

Mr Stamler argued that he could satisfy the burden of establishing non-contractual status on three main grounds:

First, he said. the court started with an equal and opposite presumption that where ambiguous words had to be construed, they must be construed, ***contra proferentem***, and that here Kleinwort was the proponent.

The submission was rejected. The *contra proferentum* rule only applied where the wording was ambiguous. Here the wording was not ambiguous.

Second, Mr Stamler submitted that as a matter of construction the contrast between the opening words of the admittedly contractual paragraph (2) of the letter, 'We confirm', and the weaker phraseology in paragraph (B), 'It is our policy to ensure', showed that paragraph (a) was intended to be non-contractual.

Paragraph (3) was unequivocal and categorical. There was no magic in "we confirm". No greater strength would have been added to paragraph (3) if it had begun "We confirm that it is our policy...."

The wording of the crucial paragraph was completely there to constitute a contractual undertaking.

Third, Mr Stamler argued that the surrounding circumstances, and in particular the appreciation by both sides that Malaysian was not prepared to accept joint and several liability or to enter into a guarantee, strongly supported displacement of the presumption.

He submitted that if the crucial paragraph was accorded legal status, it would be equivalent to a guarantee.

That was not accepted. There was a substantial difference between a guarantee and the present kind of paragraph.

A guarantee was usually drawn in language the meaning of which was not susceptible to much debate. It usually contained. detailed and stringent provisions to facilitate prompt enforcement in case of default. And it usually gave rise to a straightforward monetary claim for a precisely ascertainable figure enforceable under Order 14.

By contrast, a paragraph of the present kind often provoked debate as to its construction. Order 14 proceedings might he problematical. Morever, the claim would not be for a liquidated sum, but for damages. The underlying premise on which the argument was based was that once a formal guarantee had been rejected by Malaysian there was no further scope for a contractually binding obligation.

That was not acceptable. The one simply did not follow the other, particularly having regard to the normal characteristics of negotiations of the present kind, where parties rarely succeeded in obtaining their full objectives, but tried to obtain terms as near as possible thereto. None of Mr Stamler's, three points carried conviction.

On the other side a number of considerations strongly reinforced the presumption of a legally binding obligation:

(a) Kleinwort clearly acted in reliance inter alia on the paragraph when agreeing to advance £5m and then £10m;

(b) it was of paramount importance to Klelnwort that Malaysian should ensure that Metals was at all times in a position to meet its liabilities.

(c) it was also treated as a matter of importance by Malaysian's directors, as was shown by their formal resolution.

In business matters it was a prerequisite for-defeating the presumption of contractual status that the contrary was expressed "so precisely that outsiders might have no difficulty in understanding what they mean" (Lord Justice Scrutton in *Rose vs Frank (1923) 2KB 261):*

The crucial paragraph signally failed that test. On its proper construction in its context it did have contractual status.

There was a plain breach of contract for which Klelnwort was entitled to recover damages. Judgment for Kleinwort for £10m plus interest.

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For Kleinwort Mark Waller QC and Nicholas Padfield (Herbert Smith)

For Malaysian Samuel Stamler QC and Julian Gibson. Watt (Freshfields
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