1989 WL 649870 (CA), [1989] 1 All E.R. 785, [1989] 1 W.L.R. 379, (1989) 86(16) L.S.G. 35, (1989) 139 N.L.J. 221, (1989) 133 S.J. 262
(Cite as: [1989] 1 Lloyd's Rep. 556)

***556** Kleinwort Benson Ltd. v. Malaysia Mining Corporation Berhad

Court of Appeal

CA
Dec. 13 and 14, 1988; Feb. 2, 1989

Before Lord Justice Fox, Lord Justice Ralph Gibson , and Lord Justice Nicholls

Contract - Letter of comfort - Dealings on London Metal Exchange - Defendants furnished plaintiffs with letter of comfort as part of loan facility made by plaintiffs to subsidiary of defendants - Collapse of tin market - Plaintiffs demanded payment - Whether letter of comfort had contractual status - Whether defendants liable.

In 1983 the defendants (MMC) formed MMC Metals Ltd. (Metals) a wholly owned subsidiary to operate as a ring-dealing member of the London Metal Exchange. Metals required extra funding and there was in due course an acceptance credit/multi currency cash loan facility made available by the plaintiffs (KB) to Metals.

On Aug. 21, 1984, as part of the facility granted to Metals to a maximum of $5,000,000, MMC furnished to KB a letter of comfort which provided inter alia:

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

Subsequently the maximum amount of the facility was increased to $10,000,000 and a second and operative letter of comfort dated May 7, 1985 was furnished by MMC to KB.

The tin market collapsed and Metals ceased trading. On Nov. 11 KB terminated the facility and demanded immediate payment of all outstanding bills, loans and other sums payable which in the circumstances would not be forthcoming from Metals.

On Nov. 12, 1985 KB drew MMC's attention to Metals' default, referred to the letter of comfort and requested MMC to ensure that KB received the payments due to them.

By telex dated Dec. 3, 1985 MMC contended that the letter of comfort was not contractual and that MMC had not given any assurances that Metals would at all times be kept in a position to meet its liabilities to KB.

Held, by Q.B. (Com. Ct.) (HIRST, J.), that

(1) the two comfort letters came into existence as part and parcel of a commercial banking transaction and the paragraph in question was an important feature of those letters; the presumption that in the absence of any expression to the contrary a commercial agreement was deemed to be legally binding applied;

***557** (2) the wording of the paragraph was unequivocal and categorical and the phraseology was fully apt to express a legal obligation;

(3) there was a substantial difference between a guarantee and the paragraph in the letter of comfort; and the submission, that once a formal guarantee had been rejected by MMC (as it had) there was no further scope for the possibility of any contractually binding obligation of the sort enshrined in the paragraph, would be rejected; the one did not follow the other having regard to the normal characteristics of the negotiations;

(4) KB clearly acted in reliance inter alia on this paragraph in agreeing to advance first $5m. and then $10m.; it was of paramount importance to KB that MMC should ensure that Metals were at all times in a position to meet their liabilities under the facility arrangements and it was also treated as a matter of importance by MMC;

(5) the paragraph on its proper construction did have contractual status;

(6) the paragraph was crystal clear; it was an undertaking that now and at all times in the future so long as Metals were under any liability to KB under the facility arrangements it was MMC's policy to ensure that Metals was in a position to meet those liabilities; the plaintiffs were entitled to recover damages for breach of contract; there would be judgment for the plaintiffs.

MMC appealed.

Held, by C.A. (FOX, RALPH GIBSON and NICHOLLS, L.JJ.), that

(1) the defendants (MMC) made a statement as to what their policy was and did not in the paragraph in question of the comfort letter (i.e. par. 3) expressly promise that such policy would be continued in the future (*see* p. 563, col. 1);

(2) the concept of a comfort letter to which the parties had resort when the defendants (MMC) refused to assume joint and several liability or to give a guarantee, was known by both sides at least to extend to or include a document under which

MMC would give comfort to KB by assuming not a legal liability to ensure repayment of the liabilities of its subsidiary but a moral responsibility only; the comfort letter was drafted in terms which in par. 3 did not express any contractual promise and which was consistent with being no more than a representation of fact; there was nothing in the evidence to show that as a matter of commercial probability or common sense the parties must have intended par. 3 to be a contractual promise which was not expressly stated rather than a mere representation of fact which was so stated (*see* p. 564, col. 2; p. 565, cols. 1 and 2);

(3) it was impossible to hold that the words in par. 3 were intended to have any effect between the parties other than in accordance with the express words used; the words in par. 3 could not be regarded as intended to contain a contractual promise as to the future policy of MMC (*see*p. 566, col. 2; p. 567, col. 1);

(4) the defendants (MMC) had demonstrated that they made no relevant contractual promise to KB which could support the judgment in favour of KB; the appeal would be allowed (*see* p. 567, col. 2).

The following cases were referred to in the judgment of Lord Justice Ralph Gibson:

Chemco Leasing S.P.A. v. Rediffusion Plc, (Unreported) (C.A.) Dec. 11, 1986; July 19, 1985;

Edwards v. Skyways Ltd., [1964] 1 W.L.R. 349;

Esso Petroleum Co. Ltd. v. Mardon, (C.A.) [1976] 2 Lloyd's Rep. 305; [1976] Q.B. 801;

Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd., (H.L.) [1963] 1 Lloyd's Rep. 485; [1964] A.C. 465;

Heilbut Symons & Co. v. Buckleton (H.L.) [1913] A.C. 30;

Maclaine Watson & Co. Ltd. v. Department of Trade and Industry (C.A.) [1988] 3 W.L.R. 1033;

Prenn v. Simmonds, (H.L.) [1971] 1 W.L.R. 1381;

Rose and Frank Co. v. J. R. Crompton and Bros. Ltd., (C.A.) [1923] 2 K.B. 261.

This was an appeal by the defendants, Malaysia Mining Corporation Berhad from the decision of Mr. Justice Hirst ([1988] 1 Lloyd's Rep. 556 given in favour of the plaintiffs Kleinwort Benson Ltd. and holding in effect that the letter of comfort issued by the defendants to the plaintiffs was a letter of undertaking that the defendants would be liable for the liabilities of their subsidiary.

Representation

Mr. Mark Waller, Q.C. and Mr. Nicholas Padfield (instructed by Messrs. Herbert Smith) for the plaintiffs; Mr. Samuel Stamler, Q.C. and Mr. Julian Gibson-Watt (instructed by Messrs. Freshfields) for the defendants.

The further facts are stated in the judgment of Lord Justice Ralph Gibson.

Judgment was reserved.

Thursday Feb. 2, 1989

JUDGMENT

Lord Justice RALPH GIBSON:

This is an appeal by the defendants, Malaysian Mining Corporation Berhad, from the decision of Mr. Justice Hirst of Dec. 21 1987 ([1988] 1 Lloyd's Rep. 556), by which the plaintiffs, Kleinwort Benson Ltd., obtained judgment for damages***558** for breach of contract against the defendants for << PoundsSterling>>12.26m. including interest. The defendants ask that the judgment be set aside and that the plaintiffs' claim be dismissed on the ground that the defendants did not enter into any relevant contractual obligations to the plaintiffs.

The judgment of Mr. Justice Hirst ([1988] Lloyd's Rep. 556), contains an account of the circumstances in which the defendants provided to the plaintiffs the "comfort letter" upon the terms of which the plaintiffs' claim is founded. The description of the document as a "comfort letter" is that used by the parties themselves in the negotiations which preceded the provision of it by the defendants.

The plaintiffs are merchant bankers of high reputation and long experience. The defendants are a public limited company incorporated under the laws of Malaysia in which the Republic of Malaysia has at all material times held a controlling interest. In 1983 the defendants caused to be incorporated under the laws of this country a company called MMC Metals Ltd. ("Metals"), as a

wholly-owned but indirect subsidiary, to operate as a ring dealing member of the London Metal Exchange. The paid up capital of Metals was << PoundsSterling>>1.5m. To carry out trading upon the London Metal Exchange much larger funds would be required. There were negotiations for the provision of funds by the plaintiffs to Metals. The plaintiffs sought from the defendants assurances as to the responsibility of the defendants for the repayment by Metals of any sums lent by the plaintiffs. A "comfort letter" dated Aug. 21, 1984 was provided by the defendants as part of an acceptance credit/multi- currency cash loan facility granted by the plaintiffs to Metals to a maximum of <<PoundsSterling>>5m. That letter contained, among other statements, the assertion by the defendants that -

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

This case turns upon the proper construction, in its context, of that assertion by the defendants. In 1985 the facility was increased by the plaintiffs to a maximum of <<PoundsSterling>>10m. in reliance upon a second comfort letter dated May 7, 1985, which was in substantially identical terms.

In October, 1985 the tin market collapsed when the International Tin Council announced that it was unable to meet its liabilities which ran to hundreds of millions of pounds. An account of those events and a list of the sovereign States (including the United Kingdom and Malaysia) which were members of the I.T.C. can be found in the judgment of Lord Justice Kerr in Maclaine Watson & Co. Ltd. v. Department of Trade and Industry, [1988] 3 W.L.R. 1033. When the tin market collapsed Metals ceased trading. The plaintiffs demanded repayment of all sums outstanding. Nothing was paid, and Metals went into liquidation. The plaintiffs called upon the defendants to ensure that the plaintiffs received payment of the sums due.

The defendants refused to pay and said by telex of Dec. 3, 1985:

. . . We have been advised that the statements made in the letter of 7th May (1985) were not intended by either party to impose, and do not impose, any legally binding obligation on us to support M.M.C. Metals Ltd. You will appreciate that circumstances are now materially different from those existing at the date of that letter and that although the policy referred to was our policy at that time and in the light of the circumstances then prevailing, no assurance was given that such policy would not be reviewed in the light of changing circumstances.

We therefore cannot accept, as you stated in your telex, that we have given any assurances to you that M.M.C. Metals Ltd. would at all times be kept in a position to meet its liability to you.

Mr. Justice Hirst described in his judgment the course of the discussions between the defendants and the plaintiffs which led to the provision of the two comfort letters. Before Mr. Justice Hirst and in this Court it was accepted by both sides that those events could properly be taken into account as part of the context in which the second comfort letter was sent by the defendants.

I will set out Mr. Justice Hirst's description of those events substantially in his words which have been accepted as full and accurate by the parties: (p. 557):

. . . in the first instance, by letter dated Dec. 16, 1983, KB offered to both MMC and Metals jointly a facility totalling <<PoundsSterling>> 5m. on terms that, throughout the currency of the facility, both should be jointly and severally liable for all amounts due to KB; on this basis an accepting commission/margin of [FN1] per cent. per annum was proposed.

FN1 Fraction goes here

On Feb. 9, 1984, there was a meeting in Singapore, attended on KB's side by Mr. Gordon Irwin, who was the sole witness at the trial. At this stage KB were proposing a guarantee by MMC rather than joint and several liability, but one of MMC's represen-***559** tatives at the meeting stated that it was MMC's policy not to guarantee their subsidiary's borrowings. At a subsequent meeting in London on June 21, 1984, Mr. John Green, who had been newly appointed as the director in charge of Metals' operations, is recorded in KB's meeting note as having stated:

The original offer was outlined (<<PoundsSterling>>5m. u.f.n. @ [FN2] per cent. per annum margin guaranteed by (MMC)). A facility of this sort appears to fit in with Green's requirements, with the exception of the guarantee. Green said that (the defendants were) now not so keen on issuing guarantees just to keep finance costs down by [FN3] per cent. per annum and Green himself would be recommending that all Metals bank lines should be covered by a letter of comfort, rather than by a guarantee. I said that a letter of comfort would not be a problem, but that we would probably have to charge a higher rate.

FN2 Fraction goes here

FN3 Fraction goes here

This was reported by Mr. Irwin in an internal memorandum dated July 3, 1984 as follows:

Contrary to earlier reports, MMC have now taken a decision not to issue guarantees to cover the banking facilities granted to Metals. As a result, we have been asked to consider a line which would be covered by a letter of comfort from MMC.

Mr. Irwin in evidence accepted that by this stage he realised that KB would not be able to obtain either joint and several liability as originally proposed, or a guarantee from the defendants.

Originally it was proposed that MMC should draft the comfort letter, but eventually on July 11, 1984 KB furnished to Metals a revised facility letter addressed to them only, providing for 1/2 per cent. commission (i.e. an increase of one-eighth) and accompanied by a draft of a proposed comfort letter, in which the crucial paragraph read:

It is our policy to ensure that the business of MMC Metals Limited is *conducted in such a way that MMC Metals Ltd.* is at all times in a position to meet its liabilities to you under the above arrangements.

i.e., containing at this stage some extra words in the second line. On Aug. 10 1984 at a board meeting of MMC the following directors' written resolution was passed:

That MMC Metals Limited be authorised to accept the above facility on terms and conditions contained in the letter from Kleinwort Benson Limited [KBL] dated July 11 1984, and that the required Letter of Comfort in the form attached be issued to [KBL].

Eventually, on Sept. 17, 1984, Metals returned the formal facility letter to KB, accompanied by the first comfort letter, dated Aug. 21, 1984, with the curcial paragraph redrafted by MMC. The full text of the letter is:

We refer to your recent discussion with MMC Metals Limited as a result of which you propose granting MMC Metals Limited: (a) banking facilities of up to <<PoundsSterling>>5 million; and (b) spot and forward foreign exchange facilities with a limitation that total delivery in cash will not on any one day exceed <<PoundsSterling>>5 million.

[1] We hereby confirm that we know and approve of these facilities and are aware of the fact that they have been granted to MMC Metals Limited because we control directly or indirectly MMC Metals Limited.

[2] We confirm that we will not reduce our current financial interest in MMC Metals Limited until the above facilities have been repaid or until you have confirmed that you are prepared to continue the facilities with new shareholders.

[3] It is our policy to ensure that the business of MMC Metals Limited is at all times in a position to meet its liabilities to you under the above arrangements. Yours faithfully, MALAYSIA MINING CORPORATION BERHAD.

I have inserted numbers for the three main paragraphs for clarity of reference in this judgment. Paragraph (2) was, as is common ground, contractual.

Mr. Justice Hirst was referred to four authorities, which in order of date, were Rose and Frank Co. v. J. R. Crompton and Bros. Ltd. and Others, [1923] 2 K.B. 261, C.A.; Edwards v. Skyways Ltd., [1964] 1 W.L.R. 349, Mr. Justice Megaw; Prenn v. Simmonds, [1971] 1 W.L.R. 1381 H.L. (E) and Chemco Leasing S.P.A. v. Rediffusion Plc(unreported) July 19 1985, Mr. Justice Staughton, and Dec. 11, 1986 C.A..

From those cases, and from a passage in Chitty on Contract, 25th ed. 1983, par. 123, Mr. Justice Hirst accepted the following principles as applicable (I have separated them into numbered paragraphs):

(i) An agreement, even though it is sup-***560** ported by consideration, is not binding as a contract if it was made without any intention of creating legal relations;

(ii) In the case of an ordinary commercial transaction it is not normally necessary to prove that the parties in fact intended to create legal relations: the onus of proving that there was no such intention -

. . . is on the party who asserts that no legal effect is intended and the onus is a heavy one . . . [per Mr. Justice Megaw, in Edwards v. Skyways Ltd.].

(iii) To decide whether legal effect was intended, the Courts normally apply an objective test; for example, where the sale of a house is *not* "subject to contract", either party is likely to be bound even though he subjectively believed that he would not be bound until the usual exchange of contracts had taken place;

(iv) The Court will, in deciding that question, attach weight (a) to the importance of the agreement of the parties, and (b) to the fact that one

of them has acted in reliance upon it;

(v) In the search for agreed terms of a commercial transaction, businessmen may adopt language of deliberate equivocation in the hope that all will go well. It may, therefore, be artificial to try to ascertain the common intention of the parties as to the legal effect of such a claim if in fact their common intention was that the claim should have such effect as a Judge or arbitrator should decide: see per Mr. Justice Staughton in Chemco Leasing S.P.A. v. Rediffussion Plc, cited by Mr. Justice Hirst at p. 560. Nevertheless, the Court's task is to ascertain what common intentions should be ascribed to the parties from the terms of the documents and the surrounding circumstances.

Before stating the steps by which, having regard to those principles, Mr. Justice Hirst made his decision in this case, I must refer to three matters which Mr. Justice Hirst listed as having been relied upon by the defendants as demonstrating that the parties did not intend words in par. 3 of the comfort letter to have legal effect as a contractual term. They were:

(i) that the comfort letter should be construed against the plaintiffs as the party putting forward the paragraph in question: i.e. contra proferentem;

(ii) that the language of the paragraph was not apt to express a legal obligation and was, in that regard, markedly different from those parts of the comfort letter which did express legal obligation, and in particular the preceding par. 2, and

(iii) that the common appreciation by both sides that the defendants were not willing either to assume joint and several liability, or to enter into a guarantee, supported displacement of the presumption.

The steps by which Mr. Justice Hirst reached his conclusion may, I think, be summarized as follows:

(a) The two comfort letters came into existence as part of a commercial banking transaction and the statement in par. 3 of the letter of May, 1985 was an important feature of them.

(b) Accordingly, the presumption laid down by Edwards v. Skyways Ltd. applied and the burden therefore lay on the defendants to show that the parties did not intend par. 3 in the letter to have legal effect as a contractual term.

(c) The three matters relied upon by the defendants were not sufficient to displace that presumption:

(i) As to construction contra proferentem, that principle was not applicable because the wording was not ambiguous; and, if it was, the paragraph was the product of joint drafting and was not for this purpose to be regarded as drafted by the plaintiffs.

(ii) As to the language of the paragraph, it was fully apt to express a legal obligation.

Mr. Justice Hirst continued (at p. 562):

. . . I see no magic in the opening words "we confirm that we will not . . . " in par. (2), or their omission from par. (3): put another way, I do not think that any greater strength would have been added to par. (3) if it had begun "We confirm that it is our policy . . . "

(iii) As to the common appreciation by both sides that the defendants were not willing either to assume joint and several liability or to enter into a guarantee, that argument came "perilously close to infringing the principles that the course of negotiations cannot be invoked in order to influence the construction of the written document". Apart from that consideration the argument was unconvincing because the provisions of par. 3 are not to be equated with a guarantee even though, as it happens, the measure of damages for breach of the term contained in the paragraph would be equivalent to the amount recoverable on a guarantee. There was, in the Judge's view, a very substantial difference between, on the one hand, a guarantee, and on the other, a paragraph like the one under consideration in the present case. Further, the underlying premise upon which the argument was based was unacceptable, namely, the suggestion that once a formal guarantee had been rejected by the defendants, as it was,***561** there was no further scope for the possibility of any contractually binding obligation of the sort enshrined in par. 3.

(d) A number of considerations strongly reinforced the presumption that the parties intended that the paragraph should have legal effect, namely: (i) the plaintiffs acted in reliance on the paragraph in agreeing to advance money to Metals; (ii) it was of paramount importance to the plaintiffs that the defendants should ensure that Metals were at all times in a position to meet their liabilities; and (iii) the statement contained in par. 3 was also treated as a matter of importance by the defendants, as was shown by their formal board resolution.

Having thus held that the defendants had not

demonstrated that the parties did not intend par. 3 to have effect as a contractual term, Mr. Justice Hirst considered the interpretation of the words in par. 3. The interpretation was, in his view, crystal clear without embellishment. It was he said:

. . . an undertaking that, now and at all times in the future, so long as Metals are under any liability to the plaintiffs under the facility arrangements, it is and will be MMC's policy to ensure that Metals is in a position to meet those liabilities.

Mr. Stamler's submissions in this Court, for the defendants, were as follows. He referred to the use of letters of comfort in banking over recent years, and to the description of that practice in the book by Mr. Philip Wood: Law and Practice of International Finance, 1980, from which Mr. Justice Staughton cited passages in Chemco Leasing S.P.A. v. Rediffusion Plc. He contended that the paragraphs of the comfort letter in this case are typical of a comfort letter, both in substance and in sequence, namely: (i) a statement of the awareness of the parent company of the advances made to the subsidiary; (ii) a promise that the parent will not, without the consent of the bank, relinquish or reduce control of the subsidiary before repayment; and (iii) the words of comfort, stating how far the parent is prepared to go in supporting its subsidiary, often beginning "it is our intention . . . " or, "it is our policy . . . ". Mr. Stamler, however, did not contend, as I understood his argument, that the phrase "comfort letter" was shown to have acquired a precise meaning, in particular as to the limits of any legally enforceable liability which might be assumed by a parent company under such a letter, but he submitted that the phrase was generally understood to include a letter giving comfort only in the sense that the parent company assumed no legally enforceable liability to pay the debts of its subsidiary but did, in order to recognize fully its moral responsibility, acknowledge that the debts had been incurred by the subsidiary with the knowledge and approval of the parent, and state the present policy of the parent as to ensuring repayment.

The defendants have throughout acknowledged that the term in par. 2 of the present letter was a contractual promise; i.e., it was intended to have legal effect as such. The statement in par. 3, however, was not, it was submitted, a contractual promise and was not intended to have legal effect as such. It was nevertheless, in Mr. Stamler's submission, not devoid of legal significance; it was a representation of fact as to the policy of the defendants at the time that the statement was made; and the plaintiffs were entitled to rely upon it as a statement of the current policy of the defendants. If it were shown to have been untrue to the knowledge of the defendants at the time when it was made, the plaintiffs would have had a claim in deceit, but there has been no suggestion of that nature.

In addition, the plaintiffs were entitled to rely upon the representation as to the current policy of the defendants unless and until they were told that the policy had been changed. If the policy did change, without notice from the defendants so that the representation ceased to be true, and the plaintiffs thereafter relied upon it by making further advances to Metals, they would have (it was said) "a cause of action in misrepresentation", but no cause of action in contract. Since the contract into which the plaintiffs entered in reliance upon the representation was not made with the defendants, there could be no claim under s. 2 of the Misrepresentation Act, 1967, but a claim for negligent misrepresentation might be advanced upon the principles stated in Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd., [1963] 1 Lloyd's Rep. 485; [1964] A.C. 465. No such claim, of course, has been advanced in this case.

The main attack upon the analysis and reasoning of the learned Judge, which Mr. Stamler developed, was directed at the application by Mr. Justice Hirst of the proposition, illustrated by Edwards v. Skyways Ltd., that a promise, made for consideration in a commercial transaction, will be taken to have been intended to have contractual effect in law, unless the contrary is clearly shown. The proposition was not disputed on behalf of the defendants before Mr. Justice Hirst, or this Court. It was, however, submitted that the principle is of***562** no assistance in deciding whether, upon the evidence and upon their true construction, the words in question are words of promise or not.

On that question, it was said, neither Rose and Frank Co. v. J. R. Crompton and Bros. Ltd., nor Edwards v. Skyways Ltd. laid down any relevant presumption in favour of the plaintiffs which the defendants were called upon to displace. The Judge, it was said, was led into the belief that, if he took the view that the defendants had failed to displace the presumption laid down in Edwards v. Skyways Ltd., it followed that par. 3 was to be given effect in law as a contractual promise.

That approach was demonstrated, it was said, by the passage near the beginning of the judgment, where Mr. Justice Hirst said:

The main question . . . is whether . . . the crucial paragraph . . . was contractual in status; if it is, the subsidiary question arises as to its proper

construction.

It was, Mr. Stamler argued, further demonstrated by the summary treatment of the question of construction itself where, as set out above, the learned Judge found the answer to be crystal clear and the meaning to be an undertaking that -

. . . now and at all times in the future . . . it is and will be the defendants' policy to ensure that Metals is in a position to meet those liabilities.

For the rest, the substance of the submissions advanced by Mr. Stamler, in which he adopted the comments of Mr. Brian Davenport, Q.C., published in Lloyd's Maritime and Commercial Law Quarterly, 1988, p. 290, was as follows:

(i) The words in par. 3 are not words of contractual promise. In that respect they differ markedly from the wording of par. 2:

We confirm that we will not reduce our current financial interest in Metals . . .

(ii) To give to the words the meaning which the Judge held them to have requires that no force be given to the words "it is our policy . . ." Further, or in the alternative, it is necessary to imply, in addition to the statement as to present policy, a promise that the policy will not be changed and such an implication is not possible on the evidence in this case.

(iii) Therefore, without recourse to any assistance from the circumstances in which the transaction was conducted, it should be held that by par. 3 the defendants did not make the promise which the Judge extracted from the words.

(iv) If any doubt could be entertained as to the meaning of par. 3, that doubt should be dispelled by giving due weight to the facts proved, namely, that the plaintiffs had sought to obtain either joint and several liability of the defendants, or a guarantee from the defendants of the liabilities of Metals to the plaintiffs, and the defendants had refused to assume either form of obligation; and the plaintiffs knew that, if the transaction was to proceed, it must be without such security. Further the plaintiffs had, in compensation for not having that security, stipulated for, and obtained from Metals, the right to an increased commission of [FN4] per cent. To put some financial meaning into that point, Mr. Stamler calculated that if the facility had been revolved four times a year on the basis of 90-day bills (see cl. 2: Drawings, at p. 7, p. 23 of bundle B) the increase of [FN5]per cent. would be chargeable on << PoundsSterling>>40 million, i.e. <<PoundsSterling>>50,000 per annum.

FN4 Fraction goes here

FN5 Fraction goes here

The submission in this Court for the plaintiffs, as advanced by Mr. Waller, can be more shortly stated because Mr. Waller adopted and relied upon the reasoning of the learned Judge. As to the effect and meaning to be given to par. 3, his main submissions were that:

(i) The statement in par. 3 was made in a commercial contractual document and it is to be treated as a contractual promise if it appears on the evidence to have been so intended: see Esso Petroleum Co. Ltd. v. Mardon, [1976] 2 Lloyd's Rep. 305; [1976] 1 Q.B. 801.

(ii) It is shown to have been so intended because the statement was made for the purpose of inducing the plaintiffs to enter into the acceptance credit transaction with Metals under the credit facility and it was plainly of decisive commercial importance to the transaction;

(iii) The statement as to present policy must be taken as including a promise that that policy will remain in force. This proposition can be tested, it was said, by taking an example remote from banking: Suppose a shop, by notice, announced that "it is our policy to take back all goods purchased and to refund the price, without any questions, upon return of the goods in good condition within 14 days of purchase". If a customer should return goods, having bought them in reliance upon the notice, the shop could not (said Mr. Waller) refuse to refund the price upon the ground that the notice only stated the shop's policy on the day of purchase so that the shop was free to change its policy within the 14-day period. So in this case it is absurd in commercial terms for the defendants to claim to be free to change their announced policy after money has been advanced in reliance upon it. To treat the words of par. 3 as***563** no more than a representation of fact is to give no force to the words "at all times".

For my part, I am persuaded that the main criticisms of the judgment of Mr. Justice Hirst advanced by Mr. Stamler are well founded and I would, for the reasons which follow, allow this appeal. In my judgment the defendants made a statement as to what their policy was, and did not in par. 3 of the comfort letter expressly promise

that such policy would be continued in future. It is impossible to make up for the lack of express promise by implying such a promise, and indeed, no such implied promise was pleaded. My conclusion rests upon what, in my judgment, are the proper effect and meaning which, on the evidence, are to be given to par. 3 of the comfort letters.

Before expressing my reasons for that conclusion, I should refer to the way in which the question of "intention of creating legal relations" was introduced into this case. The plaintiffs' primary pleaded contention was that by the first letter of Aug. 21 1984, on its true construction, the defendants warranted that, in consideration of the plaintiffs' granting the facility to Metals, the defendants would ensure that Metals were at all times capable of fulfilling their financial obligations to the plaintiffs under the facility. The alternative and secondary contention was that, if the defendants had not given that warranty, the defendants warranted that it was their business policy to ensure that Metals would always have sufficient means to meet their liabilities to the plaintiffs under the terms and conditions of the facility and that, in all the circumstances, the defendants impliedly warranted that they would give to the plaintiffs reasonable notice of their intention to change that business policy.

Those two contentions were repeated with reference to the letter of May, 1985. The Judge made no findings on the secondary contention, and no alternative claim has been pursued in this Court. It is to be noted that the only reliance upon implied obligation was in that alternative claim which has not been pursued - no doubt because there is nothing to show that any failure to give notice of the change in policy caused loss to the plaintiffs.

In answer to the plaintiffs' claims, the defendants pleaded that -

> . . . the letters of 21st August 1984 and of May 1985 were, and were agreed and understood by both parties to be "letters of comfort" or "letters of awareness" falling short of any legal . . . warranty, and that the said statements of policy by the defendants (if given honestly, which they were) were not and were agreed and/or understood by both parties not to be, legally enforceable.

The defendants added that, if par. 3 of the letters constituted any actionable representation, it was only a representation of the defendants' policy or intention at the date of the letter and the defendants' only obligation was to notify the plaintiffs within a reasonable time of any change in such policy or intention.

Particulars were requested and provided of the "agreement or understanding " on which the defendants relied. In short, the defendants said that, by reference to the course of the negotiations set out by Mr. Justice Hirst in his judgment, the plaintiffs -

> . . . agreed to accept a letter of comfort (rather than any legal liability on the part of the defendants) in consideration of the increased acceptance commission.

There were thus included in the pleaded case of the defendants two distinct pleas as to the intentions of the parties with reference to par. 3 of the comfort letters. The first was that even if, upon its true construction, it contained what would have been a contractual promise, as contrasted with a mere representation of fact, nevertheless it should not be enforced as a contractual promise because there had been a separate agreement or understanding that it should not be legally enforceable.

The second plea was that, failing proof of that separate agreement or understanding, the statement in par. 3 of the comfort letters was not in its terms a warranty or contractual promise and was not intended to be such. This second plea is, in this case, inseparable, in my judgment, from the question of the proper construction of the words of par. 3 in their context although, of course, there might be in some cases a separate issue of construction once it was established that words, not in express promissory terms, were intended as a warranty. In this case, if the Court is persuaded that the statement in par. 3 as to what the policy of the defendants is, is to be treated as including a promise as to what that policy would be in future, there was not any real dispute as to what were the extent and meaning of that promise.

In the event, at the trial there was no evidence to support the first plea, i.e., that there had been an agreement that the words of the comfort letters should not have legal effect. The parties had referred to a "comfort letter ", but it was not proved that the parties had agreed on any specific meaning for that phrase as descriptive of the liabilities to be undertaken by the***564** defendants. The point was apparently not pursued. The argument concentrated on whether par. 3 was to be treated in law as a contractual promise: Mr. Justice Hirst referred to the main question as being whether par. 3 was "contractual in status", and his conclusion was, as I have said, that the presumption laid down in Edwards v. Skyways Ltd. applied and that the defendants had failed to displace the presumption.

Mr. Waller, before Mr. Justice Hirst, had placed strong reliance on Edwards v. Skyways Ltd., and his submission was recorded by Mr. Justice Hirst as follows:

There was a heavy onus on the defendants to prove that there was no intention to create contractual relations.

In my judgment Mr. Stamler is right in his submission that the presumption described in Edwards v. Skyways Ltd., had no application to the issues in this case once the plea of a separate agreement or understanding to the effect that the comfort letters should have no legal effect had disappeared from the case for want of evidence to support it. The introduction of that plea into the case appears to have served only to distract attention from what, if I am right, are the clear merits of the defendants' case as to the meaning and effect of par. 3 of the comfort letters.

To explain why, in my view, the presumption applied by Mr. Justice Hirst had no application to this case it is necessary to examine in some detail the issues in Edwards v. Skyways Ltd. In that case Skyways Ltd., the defendants, found it necessary to declare redundant some 15 per cent. of the pilots in their employ. The secretary of Skyways Ltd., at a meeting with representatives of the Air Pilots Union, agreed that -

. . . pilots declared redundant and leaving the company would be given an *ex gratia* payment equivalent to the company's contribution to the pension fund and [in addition] . . . a refund of their own contributions to the fund.

Edwards, in reliance upon that agreement, left the company and claimed payment under it. The company purported to rescind its decision to make the ex gratia payment on the ground that it had obligations to creditors and the promised ex gratia payments were not enforceable in law. The company admitted that a promise had been made to make the payments (see p. 354) and that the promise was supported by consideration, but contended (in reliance upon Rose and Frank Co. v. J. R. Crompton and Bros Ltd., [1923] 2 K.B. 261 at p. 288) that the promise or agreement had no legal effect because there was no intention to enter into legal relations in respect of the promised payment. It was argued (see p. 356) that the mere use of the phrase "ex gratia", as part of the promise to pay, showed that the parties contemplated that the promise when accepted would have no binding force in law and, further, that there was background knowledge, concerned with the tax consequences of legally enforceable promises to pay, and present to the minds of the representatives of the parties, which gave unambiguous significance to the words "ex gratia" as excluding legal relationships. Mr. Justice Megaw rejected these arguments upon the facts and upon his construction of the meaning in the context of the words "ex gratia". The company thus failed to show that what was otherwise admittedly a promise, supported by consideration, was to be denied legal effect because of the common intention of the parties that it should not have such effect and, accordingly, the company failed to displace the presumption. Mr. Justice Megaw was not dealing with the sort of question which is raised in this case, namely, whether, given that the comfort letter was intended to express the legal relationship between the parties, the language of par. 3 does or does not contain a contractual promise.

The central question in this case, in my judgment, is that considered in the case of Esso Petroleum Co. Ltd. v. Mardon, upon which Mr. Waller relied in this Court but which was not cited to Mr. Justice Hirst. That question is whether the words of par. 3, considered in their context, are to be treated as a warranty or contractual promise. Paragraph 3 contains no express words of promise. Paragraph 3 is in its terms a statement of present fact and not a promise as to future conduct. I agree with Mr. Stamler's submission that, in this regard, the words of par. 3 are in sharp contrast with the words of par. 2 of the letter: "We confirm that we will not, etc". The force of this point is not limited, as Mr. Justice Hirst stated it, to the absence from par. 3 of the words "We confirm". The real contrast is between the words of promise, namely, "We will not" in par. 2, and the words of statement of fact "it is our policy " in par. 3. Mr. Justice Hirst held that, by the words of par. 3, the defendants gave an undertaking that now and at all times in the future, so long as Metals should be under any liability to the plaintiffs under the facility arrangements, it is *and will be* the defendants' policy to ensure that Metals is in a position to meet their liabilities. To derive that meaning from the words it***565** is necessary to add the words emphasized, namely, "and will be ", which do not appear in par. 3. In short, the words of promise as to the future conduct of the defendants were held by Mr. Justice Hirst to be part of the necessary meaning of the words used in par. 3. The question is whether that view of the words can be upheld.

The absence of express words of warranty as to present facts or the absence of express words of promise as to future conduct does not conclusively exclude a statement from the status of warranty or promise. According to the well known dictum of Holt C.J.-

. . . an affirmation can only be a warranty provided it appears on evidence to have been so intended . . .

see Lord Justice Ormrod: Esso Petroleum Co. Ltd. v. Mardon, [1976] 2 Lloyd's Rep. 305 at p. 313; [1976] 1 Q.B. 801 at p. 824G, citing Viscount Haldane L.C. in Heilbut, Symons & Co. v. Buckleton, [1913] A.C. 30 at p. 38. Thus in Esso Petroleum Co. Ltd. v. Mardon the statement that -

. . . Esso estimated that the throughput of the site in its third year of operations would amount to <<PoundsSterling>>200,000 gallons a year . . .

which had been made as an expert estimate, which was of great commercial importance to a potential tenant of the site, and which induced Mr. Mardon to enter into the contract of lease, was held to be a warranty not that such a throughput would be achieved, but that, in effect, the estimate had been made with due care upon the basis of information in the possession of Esso: (see per Lord Denning, M.R. at p. 309, col. 2; p. 818E; Lord Justice Ormrod at p. 315, col. 1; p. 827A, and Lord Justice Shaw at p. 318, col. 2; p. 832B).

Mr. Waller in this Court placed reliance upon the decision in Esso Petroleum Co. Ltd. v. Mardon. It is, in my judgment, on the facts of this case, of no assistance to the plaintiffs. The evidence does not show that the words used in par. 3 were intended to be a promise as to the future conduct of the defendants but, in my judgment, it shows the contrary.

The concept of a comfort letter was, as Mr. Stamler acknowledged, not shown to have acquired any particular meaning at the time of the negotiations in this case with reference to the limits of any legal liability to be assumed under its terms by a parent company. A letter, which the parties might have referred to at some stage as a letter of comfort, might, after negotiation, have emerged containing in par. 3 in express terms the words used by Mr. Justice Hirst to state the meaning which he gave to par. 3. The Court would not, merely because the parties had referred to the document as a comfort letter, refuse to give effect to the meaning of the words used. But in this case it is clear, in my judgment, that the concept of a comfort letter, to which the parties had resort when the defendants refused to assume joint and several liability or to give a guarantee, was known by both sides at least to extend to or to include a document under which the defendants would give comfort to the plaintiffs by assuming, not a legal liability to ensure repayment of the liabilities of its subsidiary, but a moral responsibility only. Thus, when the defendants by Mr. John Green in June 1984 told the plaintiffs that Mr. Green would recommend that credit lines for Metals be covered by a letter of comfort rather than by guarantee, the response of Mr. Irwin, before any draft of a comfort letter had been prepared, was:

. . . that a letter of comfort would not be a problem but that he would probably have to charge a higher rate.

The comfort letter was drafted in terms which in par. 3 do not express any contractual promise and which are consistent with being no more than a representation of fact. If they are treated as no more than a representation of fact, they are in that meaning consistent with the comfort letter containing no more than the assumption of moral responsibility by the defendants in respect of the debts of Metals. There is nothing in the evidence to show that, as a matter of commercial probability or common sense, the parties must have intended par. 3 to be a contractual promise, which is not expressly stated, rather than a mere representation of fact which is so stated.

Next, the first draft of the comfort letter was produced by the plaintiffs. Paragraph 1 contained confirmation that the defendants knew of and approved of the granting of the facilities in question by the plaintiffs to Metals, and par. 2 contained the express confirmation that the defendants would not reduce their current financial interest in Metals until (in effect) facilities had been paid or the plaintiffs consented. Both are relevant to the present and future moral responsibility of the defendants. If the words of par. 3 are to be treated as intended to express a contractual promise by the defendants as to their future policy, which Mr. Justice Hirst held the words to contain, then the recitation of the plaintiffs' approval and the promise not to reduce their current financial interest in Metals, would be of no significance. If the defendants have promised that at all***566** times in the future it will be the defendants' policy to ensure that Metals is in a position to meet its liabilities to the plaintiffs under the facility, it would not matter whether they had approved or disapproved, or whether they had disposed of their shares in Metals. Contracts may, of course, contain statements or promises which are caused to be of no separate commercial importance by the width of a later promise in the same document. Where, however, the Court is examining a statement which is by its express words no more than a representation of fact, in order to consider whether it is shown to have been intended to be of the nature of a contractual promise or warranty, it seems to me to be a fact suggesting at least the absence of such intention if, as in this case, to read the statement as a contractual promise is to reduce to no significance two paragraphs included in the

plaintiffs' draft, both of which have significance if the statement is read as a representation of fact only.

That point can be made more plainly thus: if par. 3 in its original or in its final form was intended to contain a binding legal promise by the defendants to ensure the ability of Metals to pay the sums due under the facility, there was no apparent need or purpose for the plaintiffs, as bankers, to waste ink on par. 1 and 2.

As I have said, the absence of express words of promise does not by itself prevent a statement from being treated as a contractual promise. The example given in argument by Mr. Waller, namely of the shop stating by a notice that it is its policy to accept, within 14 days of purchase, the return in good condition of any goods bought, and to refund the price without question, seems to me to be a case in which a Court would be likely to hold that the notice imported a promise that the policy would continue over the 14-day period. It would be difficult on those facts to find any sensible commercial explanation for the notice other than a contractual promise not to change the policy over the 14-day period. It would not be satisfactory or convincing to regard the notice as no more than the assumption of a moral responsibility by the shop giving such a notice to its customers. In such a case, and in the absence of any relevant factual context indicating otherwise, it seems to me that the Court would probably hold that the statement was shown to have been intended to be a contractual promise.

In this case, however, the opposite seems to me to be clear. The context in which the comfort letter was requested and given is before the Court without dispute as to the relevance or admissibility of that context. That concession was, in my view, rightly made. The evidence showing the context in which the comfort letters were produced, as set out in the judgment of Mr. Justice Hirst, was evidence of the factual background known to the parties at or before the date of the contract and of the "genesis" and "aim" of the transaction: see Prenn v. Simmonds, [1971] 1 W.L.R. 1381: in short the provision of a comfort letter by the defendants, as the parent company of Metals to which the plaintiffs were intending to provide finance, in circumstances in which the defendants had refused to assume legal liability for the repayment of money lent to Metals by the plaintiffs, whether in the form of joint and several liability or of guarantee. Those facts are not available to show merely that the defendants did not themselves subjectively intend to assume legal liability and that, therefore, the words eventually included in the comfort letter provided by the defendants should be construed so as to exclude such liability. That, as I understand it, would be mis-applying the principles stated in Prenn v. Simmonds, by which evidence of the factual background is admitted. But the evidence of the refusal by the defendants to assume legal responsibility for the liabilities of Metals to the plaintiffs in the normal form of joint and several liability or of guarantee, and the consequent resort by the parties to what they described as a comfort letter substantially in the terms submitted by the plaintiffs to the defendants, is, in my judgment, admissible on the question whether, for the purposes of the test applied by this Court in Esso Petroleum Co. Ltd. v. Mardon, the defendants' affirmation in par. 3 appears on the evidence to have been intended as a warranty or contractual promise.

With that evidence before the Court I find it impossible to hold that the words in par. 3 were intended to have any effect between the parties other than in accordance with the express words used. For this purpose it seems to me that the onus of demonstrating that the affirmation appears on evidence to have been intended as a contractual promise must lie on the party asserting that it does, but I do not rest my conclusion upon failure by the plaintiffs to discharge any onus. I think it is clear that the words of par. 3 cannot be regarded as intended to contain a contractual promise as to the future policy of the defendants. If par. 3 had been drafted by the plaintiffs and submitted in the form in which Mr. Justice Hirst formulated its meaning, namely "as an undertaking that now and at all times in the future, so long as Metals are under any liability to the plaintiffs under the***567** facility arrangements, it is and will be the defendants' policy to ensure that Metals is in a position to meet their liabilities", it must have appeared to both parties, in the context proved in evidence, as a radically different term from that which was in fact submitted and accepted. Such an undertaking does not fit, as a matter of commercial probability, with the factual background. I do not suggest that people only act in accordance with apparent commercial probability; the plaintiffs might have submitted such an undertaking which, in the light of the prior refusal to give a guarantee, was likely to be rejected and the defendants - contrary to what seemed likely - might have accepted it, but the plaintiffs in fact submitted the words we see in par. 3. The plain meaning of those words, without the addition contained in Mr. Justice Hirst's formulation of its meaning, does fit the factual background. Most importantly, that factual background explains, notwithstanding the commercial importance to the

plaintiffs of security against failure by Metals to pay and the plaintiffs' reliance upon the comfort letter, why the plaintiffs drafted and agreed to proceed upon a comfort letter which, on its plain meaning, provided to the plaintiffs no legally enforceable security for the repayment of the liabilities of Metals. I therefore find it impossible to hold that by the words of par. 3 the parties must be held to have intended that the plaintiffs be given that security.

I should mention briefly some other points which were argued. As is apparent from what I have said above, the plaintiffs are, in my judgment, to be regarded as the party putting forward the language contained in the comfort letters as a whole. The change in the wording introduced by the defendants made no difference whatever to the meaning. It was not argued that it did. Mr. Justice Hirst held that the principle of construction contra proferentem had no application because there was no ambiguity. I do not agree. The question was whether words, which are not in the form of a contractual promise, are on the evidence to be treated as intended to have been such a promise. Having regard to the defendants' prior refusal to assume joint and several liability or to give a guarantee, and to the resort by the parties to what was referred to as a comfort letter, it seems to me that the defendants are entitled to rely upon the fact that, if the plaintiffs required a promise as to the defendants' future policy, it was open to them as experienced bankers to draft par. 3 in those terms. I do not, however, regard the point as decisive. If the letter in its final form is to be regarded as the result of joint drafting, my conclusion would not be affected.

Submissions were made to Mr. Justice Hirst, and repeated in this Court, as to the differences between the liability of the defendants upon a formal guarantee, and the ease of enforcement of that liability, on the one hand, and the liability and attendant problems of enforcement under par. 3, on the other hand, according to its meaning and effect as determined by the Judge.

I did not find these submissions to be of any assistance in the resolving of the main issue in this case, and I do not propose to deal with them in any detail. I agree with Mr. Justice Hirst that the mere fact that the defendants had refused to give a formal guarantee did not mean that there was no further scope for the subsequent agreement by them to a term having the meaning and effect which Mr. Justice Hirst gave to par. 3; but contemplation by either party of the alleged differences in certainty or of the availability of summary judgment seems to me to be wholly improbable.

If my view of this case is correct, the plaintiffs have suffered grave financial loss as a result of the collapse of the tin market and the following decision by the defendant company not to honour a moral responsibility which it assumed in order to gain for its subsidiary the finance necessary for the trading operations which the defendants wished that subsidiary to pursue. The defendants have demonstrated, in my judgment, that they made no relevant contractual promise to the plaintiffs which could support the judgment in favour of the plaintiffs. The consequences of the decision of the defendants to repudiate their moral responsibility are not matters for this Court.

I would allow this appeal.

Lord Justice NICHOLLS:

I agree.

Lord Justice FOX:

I also agree.

[Order: Appeal allowed with costs in the Court of Appeal and below. Leave to appeal to the House of Lords refused.]

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