

No ordinary debt claim

When Russia calls and asks you to get its money back from Ukraine

Summary

On 29 March 2017, the High Court handed down its judgment in *The Law Debenture Trust Corporation P.L.C. v Ukraine* [2017] EWHC 655 (Comm) (the **Ukraine Case**) which considered a summary judgment application by The Law Debenture Trust Corporation P.L.C. (**Law Debenture**) in respect of the non-payment of US\$3bn of Eurobonds (the **Notes**) by the State of Ukraine (**Ukraine**). Law Debenture was trustee of the Notes and was directed to bring proceedings by the Russian Federation (**Russia**) which was the sole holder of the Notes. Although Mr Justice Blair commented that the background to the case was “extraordinary”, he held that the Trustee was entitled to summary judgment as there were no valid reasons under English law to suppose that Ukraine has a real prospect of successfully defending the claim brought by Law Debenture.

Geopolitical tensions had emerged between Russia and Ukraine over the latter’s proposed signature of an Association Agreement with the European Union in November 2013. Ukraine claimed that Russia had exerted unlawful and illegitimate political and economic pressure on it in order to compel it to accede to Russian financial support instead of signing that agreement. The US\$3bn Notes represented the first part of Russian financial support. Despite Russia’s alleged annexation of the Crimean Peninsula and allegations of general interference in Ukraine’s domestic political affairs, Ukraine made three interest payments under the Notes in 2014 and 2015 before Ukrainian Ministers approved a moratorium on 18 December 2015 to suspend payment of the Notes shortly before the Notes were due to be repaid.

Ukraine’s defence

Ukraine provided four grounds of defence to the claim for payment of the Notes:

- **Capacity:** Ukraine claimed that it did not have the capacity to issue the Notes because the debt issuance contravened its own Budget Law limit and because Ukrainian Ministers were not provided with a mandatory opinion on the borrowing.
- **Duress:** Ukraine argued that Russia’s behavior, which included threats to enforce protective tariffs against Ukrainian goods and to end co-operation between the countries in a number of industries, constituted duress under English law. As a result Ukraine claimed the Notes were voidable, and were in fact avoided by the moratorium of 18 December 2015.
- **Implied Terms:** Ukraine claimed that contractual terms should be implied into the Trust Deed to the effect that Russia would not deliberately interfere with or hinder Ukraine’s ability to repay under the Notes and that Russia would not demand repayment if it breached well-established principles of international law - and that in turn Russia was in breach of those implied terms.
- **Non-Payment as a Countermeasure:** Ukraine argued that under public international law it was entitled to decline to make payments to Russia under the Notes as a proportionate “countermeasure”, taking into account the impact of Russia’s activities on its economic and territorial integrity.

It is fair to note that these are among the more unusual defences that have been raised to a claim for non-payment of a debt.

The Court's reasons for dismissing the defence

Mr Justice Blair rejected all four grounds of defence. Ukraine is a sovereign state which had entered into a debt contract governed by English law. Mr Justice Blair found that as a matter of international law, sovereign states had an unlimited capacity to borrow and that English law duly recognized such capacity. Further, the Ukrainian Minister of Finance through his governmental position had usual authority to enter into the transaction on behalf of Ukraine. The fact that the Minister of Finance was the signatory on all 31 debt issuances by Ukraine in which Law Debenture had acted as trustee between 2000 and 2013 established “such authority beyond doubt”.

Mr Justice Blair commented, obiter, that a defence of duress should not in principle be blocked off to an issuer where the transactional structure incorporates a trustee. However, Mr Justice Blair considered that the English courts did not have the competence to adjudicate either on transactions entered into between states “on the plane of international law” or on international treaties and conventions which have not become part of domestic law. Similarly, the English courts were not competent to rule on questions of aggression or armed conflict among states. In these circumstances, he held that the allegedly coercive measures by Russia relied upon by Ukraine in its defence of duress fell within the foreign act

of state doctrine and were therefore not capable of being determined by the High Court. They were in that sense “non-justiciable”.

Ukraine’s third defence failed because Mr Justice Blair held that the test for the implication of terms was not satisfied on these facts. This was primarily because, even if in some circumstances the Court will imply a term that neither party will prevent the other party’s performance, such an approach was not appropriate in a case like this where transferrable instruments such as the Notes were involved. The Judge noted that potential transferees of Notes have to be able to identify the rights which they are acquiring from the relevant contracts themselves, and that implication of the sorts of terms suggested by Ukraine would risk the Notes becoming unworkable and untradeable. Although Russia was unlikely to have intended to transfer the Notes at any point before the due date, this was not legally relevant because the test for the implication of terms is determined at the time of contracting. It is also worth noting that recent case authority on transferable debt instruments has given prominence to the express wording of contracts for similar reasons to those considered by Mr Justice Blair.

Ukraine’s argument that non-payment constituted a legitimate “countermeasure” under public international law was rejected because English courts are not competent to consider such measures.



Conclusion

In one respect the Ukraine case represents a simple debt claim under English law. As trustee of the Notes, Law Debenture was owed the debt obligation. The relevant transaction documents, including the Trust Deed and the Agency Agreement, were governed by English law. However, as Mr Justice Blair acknowledged in his judgment, the complex geopolitical backdrop to the case meant that Ukraine's four main defences in fact raised "legal questions of considerable difficulties". The length of the judgment (107 pages) speaks to these difficulties. Mr Justice Blair also took the relatively unusual step of annexing the factual sections of Ukraine's defence to his judgment so that readers are able to appreciate the context in which the court was asked to consider these matters.

As the UK forges a new relationship with its neighbors, the case reminds us that English law is the choice of many involved in cross border investment, and that the English courts will apply consistent legal principles even in the most unusual of circumstances. The case also illustrates the fact that trustees cannot choose their beneficiaries, and can find themselves fighting some unusual corners.

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