Neutral Citation Number: [2021] EWHC 1259 (Comm)

Case No: CL-2020-000533

IN THE HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION
COMMERCIAL COURT

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 19/05/2021

Before:

HIS HONOUR JUDGE PELLING QC
SITTING AS A JUDGE OF THE HIGH COURT

- -

Between:

BROWN-FORMAN BEVERAGES EUROPE, LTD	**Claimant**
- and –	
BACARDI UK LIMITED	**Defendant**

- -

Mr Charles Graham QC and Mr Alexander Brown (instructed by **Eversheds Sutherland (International) Limited**) for the **Claimant**
Mr Jonathan Davies-Jones QC and Mr Christopher Bond (instructed by **DLA Piper UK LLP**) for the **Defendant**

Hearing dates: 15-18 March 2021

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Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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HIS HONOUR JUDGE PELLING QC, SITTING AS A JUDGE OF THE HIGH COURT

HH Judge Pelling QC:

Introduction

1. This is the trial of various preliminary issues in a claim by the claimant ("BFBE") against the defendant ("BUKL") under a contract of suretyship pursuant to Paragraph 5 of a Case Management Order made on 11 December 2020 by Andrew Baker J. The issues directed to be tried are the issues identified as Issues 1 to 10 and 12(a) on the List of Issues although in practical terms these issues that arise go to three broad questions identified below. Although this is a trial, no oral evidence was adduced by either party and the trial proceeded by way of submission alone – see T1/5/14 – 6/13.

Background

2. BUKL is part of the global Bacardi group of companies and is the parent company of Bacardi-Martini Limited ("BML"). By an agreement made on 21 November 2016 entitled "AMENDED AND RESTATED UNITED KINGDOM COST-SHARING AGREEMENT" ("Agreement") the parties agreed to share costs in relation to the provision of certain services. By clause 6.2 of the Agreement:

> "Bacardi U.K. Limited agrees to guarantee the payment and related obligations of BML under this Agreement. BML agrees to cause a duly authorized officer of Bacardi U.K. Limited to execute the form of guarantee attached to, and incorporated into, this Agreement as Schedule 6.2 to document such guarantee obligations. Bacardi U.K. Limited agrees to indemnify and hold BFBE, BFC, and their respective Associated Companies, harmless from and against and in respect of any and all losses, liabilities, claims, judgments, expenses, costs (including attorneys' fees) and settlements incurred in connection with any failure by BML to timely fulfil its payment obligations to BFBE and BFC under this Agreement."

Schedule 6.2 of the Agreement, entitled "FORM OF BACARDI U.K. LIMITED GUARANTEE" it was agreed that the guarantee to be given by BUKL would be to the following effect:

> "1. Bacardi U.K. Limited shall procure that any obligation or requirement which is expressed in this Agreement to be an obligation or requirement of BML be performed or discharged.
>
> 2. In consideration of BFBE and BFC entering into and extending the amended and restated cost-sharing arrangement with BML for the United Kingdom operations on the terms set out in the Amended and Restated United Kingdom Cost-Sharing Agreement initially effective as of 1 May 2017 and valid until 30 April 2020 (the "Agreement"), Bacardi U.K. Limited hereby unconditionally and irrevocably guarantees to BFBE and BFC the due and punctual performance and observance by BML of all

> of its obligations, commitments and undertakings under or pursuant to the Agreement or any other document entered into pursuant to the Agreement.
>
> 3. If and whenever BML defaults for any reason whatsoever in the performance of any obligation, commitment or undertaking undertaken or expressed to be undertaken under or pursuant to the Agreement or any other document referred to in it, Bacardi UK. Limited shall upon demand unconditionally perform (or procure performance of) and satisfy (or procure satisfaction of) the obligation, commitment or undertaking in regard to which such default has been made in the manner prescribed by the Agreement or any other document referred to in it and so that the same benefits shall be conferred on BFBE and BFC as would have been received if such obligation, commitment or undertaking had been duly performed and satisfied by BML.
>
> 4. This guarantee is to be effective as of the date of conclusion of the Agreement and shall be a continuing guarantee and accordingly is to remain in force until all obligations of BML shall have been performed or satisfied, regardless of the legality, validity or enforceability of any provisions of the Agreement and notwithstanding the winding-up, liquidation, dissolution or other incapacity of BML or any change in the status, control or ownership of BML. This guarantee is in addition to, without limiting and not in substitution for, any rights or security that BFBE or BFC may now or after the date of the Agreement have or hold for the performance and observance of the obligations, commitments and undertakings of BML under or in connection with the Agreement or any other document referred to in it.
>
> 5. As a separate and independent stipulation, Bacardi U.K. Limited agrees that any obligation, commitment or undertaking expressed to be undertaken by BML (including, without limitation, any moneys expressed to be payable under the Agreement) which may not be enforceable against or recoverable from BML by reason of any legal disability or incapacity on or of BML or any fact or circumstance (other than any limitation imposed by the Agreement) shall nevertheless be enforceable against and recoverable from Bacardi U.K. Limited as though the same had been incurred by Bacardi U.K. Limited and Bacardi U.K. Limited were the sole or principal obligor in respect thereof and shall be performed or paid by Bacardi U.K. Limited on demand."

By clause 13.8 of the Agreement, it was agreed that:

> "As of the Effective Date, this Agreement shall supersede and cancel all prior written or oral contracts, agreements, and understandings of the parties with respect to the subject matter covered by this Agreement. This Agreement can be amended

> only in writing, and then only if the amendment is executed by all parties affected by the amendment. This Agreement is the product of arms-length negotiation between the parties and will not be construed against any party as the "drafter" of the document."

The Agreement was executed on behalf of BUKL under a statement that:

> "Bacardi UK Limited hereby signs this Agreement to agree to be bound by the obligations and undertakings set forth in section 6.2 (Parent Guarantee) and agrees to execute the Guarantee in the form attached as Schedule 6.2."

It is common ground that BUKL was not a party to the Agreement, but it signed it specifically to signify its assent to being bound by the surety obligations set out in section 6.2 and Schedule 6.2 alone.

3. On 31 January 2019, an agreement entitled "ADDENDUM AGREEMENT" ("AA") was made between BFBE, BML and BFBE's parent company ("BFC") by which the terms of the Agreement were varied. By clause 4 of the AA, it was agreed that:

> "Each of the parties agrees that it has received adequate and independent consideration for entering into this Addendum Agreement on behalf of itself and its Associated Companies. All provisions of the Agreement not subject to amendment under this Addendum remain in full force and effect."

The AA was signed on behalf of (a) BFBE, (b) its parent and (c) on behalf of BML by its managing director and by its finance director on 8 January 2019. BUKL was not a party to the AA, nor a signatory to it.

4. BML has failed to pay BFBE £51,499,402 under the terms of the Agreement. BML has refused to pay this sum on the basis that it has claims against BFBE under the Agreement, which equal or exceed the sums claimed by BFBE, that it relies on as supporting a defence of equitable set off. BFBE accepts (for the purposes of these proceedings) that BML has validly asserted its equitable set off defence reasonably and in good faith. The Agreement contains an arbitration agreement that applies as between BFBE and BML. The claim and cross claims between BML and BFBE have been referred to arbitration in accordance with that agreement.

The Issues

5. Given that the claims and cross claims between BFBE and BML are the subject of an arbitration in which (BFBE accepts for the purposes of these proceedings that) BML has pleaded a valid equitable set off, this trial is concerned with whether BUKL is liable to BFBE for the sums claimed by BFBE against BML that have been referred to arbitration under either:

   i) The third sentence of clause 6.2 of the Agreement ("the Clause 6.2 claim"); and/or

ii) Paragraph 5 of Schedule 6.2 ("the paragraph 5 claim").

- see T1/8/3-17.

6. BUKL summarises its defences to BFBE's claim to recover the sums it claims from BML in the arbitration under each of the provisions of the Agreement referred to above at paragraph 6 of its written opening as being first that it relies on BML's assertion of equitable set off on the basis of " … *the general principle that a surety may rely on an [equitable set off] asserted by the principal debtor, and as a matter of the proper construction of its obligations under the guarantee, BUKL contends that none of its obligations has been triggered* …" and independently it denies that it is liable " … *on the basis that its surety obligations were automatically discharged by a variation to the Agreement effected by* …" the AA, applying the rule in Holme v Brunskill (1878) 3 QBD 495.

7. BFBE submits that these defences should be rejected because (a) the relevant obligations are primary obligations, (b) as a matter of construction the obligation to pay under those provisions has been triggered by the refusal of BML to pay in reliance on its equitable set off defence and (c) the rule in Holme v Brunskill does not apply to primary obligations of the sort contained in either the third sentence of clause 6.2 or paragraph 5 of Schedule 6.2 and (d) even if that is wrong (i) the variation was not material and so does not trigger the rule and (ii) on a proper construction, BUKL has consented to the variation.

The True Meaning and Effect of the Third Sentence of Clause 6.2 – Issues 3, 8 and 10 in the List of Issues

8. The relevant part of clause 6.2 of the Agreement provides:

> " … Bacardi U.K. Limited agrees to indemnify and hold BFBE, BFC, and their respective Associated Companies, harmless from and against and in respect of any and all losses, liabilities, claims, judgments, expenses, costs (including attorneys' fees) and settlements incurred in connection with any failure by BML to timely fulfil its payment obligations to BFBE and BFC under this Agreement."

9. BFBE submits that this part of clause 6.2 is intended to impose a primary obligation to indemnify whereas the first and second sentences of the clause are concerned with a series of guarantees (being the provisions set out in paragraphs 1-4 of Schedule 6.2), which are secondary obligations, being guarantees in its pure form.

10. The legal consequences that flow from the distinction between an indemnity and a true guarantee are well known. Indemnities and guarantees are both contracts of suretyship. A contract of guarantee is a contractual obligation by the surety either to discharge a debt owed by the principal debtor in the event that the principal debtor does not discharge it and has not ceased to be liable to pay it; or a contractual obligation by the surety to "*see to it*" that the principal debtor complies with its guaranteed obligations with the result that if the principal fails to comply with its obligations the surety thereby is placed in breach of its contractual obligations and becomes liable in damages – see Moschi v Lep Air Services Limited [1973] AC 331 *per* Lord Reid at 344-345; Vossloh

AG v Alpha Trains UK Ltd [2010] EWHC 2443 (Ch) *per* Sir William Blackburne at paragraph 23 and Sutherland Professional Funding Limited v Bakewells [2013] EWHC 2685 (QB) at paragraph 52. As Sir William Blackburne said in Vossloh AG v Alpha Trains UK Ltd (ibid.) at paragraph 24:

> "An essential distinguishing feature of a true contract of guarantee – but not its only one - is that the liability of the surety (i.e. the guarantor) is always ancillary, or secondary, to that of the principal, who remains primarily liable to the creditor. There is no liability on the guarantor unless and until the principal has failed to perform his obligation. The guarantor is generally only liable to the same extent that the principal is liable to the creditor. This has the consequence that there is usually no liability on the part of the guarantor if the underlying obligation is void or unenforceable, or if the obligation ceases to exist (to which principle – the so-called principle of co-extensiveness - there are, however, a number of exceptions). It will depend upon the terms of the contract of suretyship whether a demand must be made on the principal or on the guarantor (or on both) in order to trigger the guarantor's obligation to pay. Many modern guarantees expressly negative the need for the creditor to make a demand on the principal or on the guarantor or to take any other given step before enforcing the guarantee."

By contrast, an indemnity obligation is a security obligation that imposes on the surety a primary obligation that is wholly independent of the liability (if any) that arises between the principal debtor and the creditor. As Sir William Blackburne stated at paragraph 26 of his judgment in Vossloh AG v Alpha Trains UK Ltd (ibid.):

> "The fact that the obligation to indemnify is primary and independent has the effect that the principle of co-extensiveness does not apply to a contract of indemnity. The indemnity not only shifts the burden of the principal's insolvency on to the indemnifier but it also safeguards the creditor against the possibility that his underlying transaction with the principal is void or unenforceable. It also prevents the discharge of the principal or any variation or compromise of the creditor's claims against the principal from necessarily affecting the liability of the indemnifier under his contract with the creditor."

11. Whilst the main differences between a guarantee and an indemnity are as set out above, into which category a particular agreement falls is a matter of construction. The principles that apply to the construction of agreements are well known. In summary:

    i) The court construes the relevant words of a contract in its documentary, factual and commercial context, assessed in the light of (a) the natural and ordinary meaning of the provision being construed, (b) any other relevant provisions of the contract being construed, (c) the overall purpose of the provision being construed and the contract in which it is contained, (d) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (e) commercial common sense, but (f) disregarding

subjective evidence of any party's intentions – see Arnold v Britton [2015] UKSC 36 [2015] AC 1619 per Lord Neuberger PSC at paragraph 15 and the earlier cases he refers to in that paragraph;

ii) A court can only consider facts or circumstances known or reasonably available to both parties that existed at the time that the contract or order was made - see Arnold v Britton (ibid.) per Lord Neuberger PSC at paragraph 21;

iii) In arriving at the true meaning and effect of a contract, the departure point in most cases will be the language used by the parties because (a) the parties have control over the language they use in a contract; and (b) the parties must have been specifically focussing on the issue covered by the disputed clause or clauses when agreeing the wording of that provision – see Arnold v Britton (ibid.) per Lord Neuberger PSC at paragraph 17;

iv) Where the parties have used unambiguous language, the court must apply it – see Rainy Sky SA v Kookmin Bank [2011] UKSC 50 [2011] 1 WLR 2900 per Lord Clarke JSC at paragraph 23;

v) Where the language used by the parties is unclear the court can properly depart from its natural meaning where the context suggests that an alternative meaning more accurately reflects what a reasonable person with the parties' actual and presumed knowledge would conclude the parties had meant by the language they used but that does not justify the court searching for drafting infelicities in order to facilitate a departure from the natural meaning of the language used – see Arnold v Britton (ibid.) per Lord Neuberger PSC at paragraph 18;

vi) If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other – see Rainy Sky SA v Kookmin Bank (ibid.) per Lord Clarke JSC at paragraph 21 - but commercial common sense is relevant only to the extent of how matters would have been perceived by reasonable people in the position of the parties, as at the date that the contract was made – see Arnold v Britton (ibid.) per Lord Neuberger PSC at paragraph 19;

vii) In striking a balance between the indications given by the language and those arising contextually, the court must consider the quality of drafting of the clause and the agreement in which it appears – see Wood v Capita Insurance Services Limited [2017] UKSC 24 per Lord Hodge JSC at paragraph 11. Sophisticated, complex agreements drafted by skilled professionals are likely to be interpreted principally by textual analysis unless a provision lacks clarity or is apparently illogical or incoherent – see Wood v Capita Insurance Services Limited (ibid.) per Lord Hodge JSC at paragraph 13 and National Bank of Kazakhstan v Bank of New York Mellon [2018] EWCA Civ 1390 per Hamblen LJ at paragraphs 39-40; and

viii) A court should not reject the natural meaning of a provision as correct simply because it appears to be a very imprudent term for one of the parties to have agreed, even ignoring the benefit of wisdom of hindsight, because it is not the function of a court when interpreting an agreement to relieve a party from a bad bargain - see Arnold v Britton (ibid.) per Lord Neuberger PSC at paragraph 20

and Wood v Capita Insurance Services Limited (ibid.) per Lord Hodge JSC at paragraph 11.

12. Neither party relies upon factual context. Both parties rely to an extent on what they characterise as commercial common sense and both parties focus primarily on the language used by the parties in the Agreement. That means that the construction issues that arise will depend on the principles summarised in paragraph 11 (i) (a), (b), (c) and (e), (iii). (iv), (v) and (vi) above. In reaching the conclusions set out below I have done so applying these principles. The only other principle that applies to contract construction that I should mention as being common ground that I should apply is that generally a court should give effect to the whole of the language used and not conclude that any part of it is surplusage unless no other conclusion is available – see T1/19/5-11. I have endeavoured to apply this principle throughout.

13. Applying those principles, I consider that the effect of the third sentence of clause 6.2 of the Agreement is to create an indemnity in the sense summarised above and not a guarantee in its pure form as summarised above. My reasons for reaching that conclusion are as follows.

14. First, there is a clear distinction drawn by the parties between what is intended to be referred to by the first sentence within clause 6.2 and what was intended to be the scope and effect of the third sentence. In my judgment that this is so is further emphasised by the express reference within the second sentence of the clause to the purpose of Schedule 6.2 being "… *to document such guarantee obligations*". This points clearly to (a) what is referred to in the first sentence being what is set out in Schedule 6.2 and (b) an intention that what follows should be in addition to what comes within the scope of the provisions set out in Schedule 6.2. There would be no logic in the third sentence merely re-stating what has been set out in Schedule 6.2, nor would there be any logic in not including the various liabilities that are referred to in the third sentence within the scope of Schedule 6.2 had what is set out in the third sentence not been intended to have additional contractual effect.

15. Secondly, the language used in the third sentence of clause 6.2 shows that what was intended to come within the scope of the third sentence was in addition to what comes within the scope of the provisions set out in Schedule 6.2. It is for that reason that it refers to losses etc " … *incurred in connection with any failure by BML to timely fulfil its payment obligations to BFBE and BFC under this Agreement ..."* none of which are referred to in any of the provisions in Schedule 6.2. Had it been intended to create an independent primary obligation on the part of BUKL to pay sums otherwise due from BML under the Agreement, it would have been entirely straightforward for the lawyers acting for the parties to have included wording to that effect in the third sentence. There is no such wording.

16. Thirdly, the language used by the parties within the Agreement shows that the parties were familiar with and distinguished as necessary between what they intended should take effect as guarantee obligations in the pure sense referred to above and those that they did not. This point has added significance given that the Agreement is a professionally drawn document. Commercial lawyers acting for entities such as the parties in this litigation will be fully familiar with the distinction between guarantees and indemnities and it is unreal to ignore that fact when considering the true meaning and effect of the provisions I am concerned with. The language used in the first sentence

of clause 6.2 and paragraphs 1 – 4 of Schedule 6.2 are unambiguously consistent with the parties intending that the obligations there referred should take effect as guarantees in the pure sense whereas the language used in both paragraph 5 of Schedule 6.2 and the third sentence of clause 6.2 is markedly different with the third sentence of clause 6.2 being expressly concerned with an indemnity in respect of what appears broadly to be consequential losses caused by a failure on the part of BML to fulfil its primary obligations, which have been guaranteed by BUKL under schedule 6.2, paragraphs 1-4.

17. Fourthly, I reject the suggestion that I should reach a different conclusion by reason of the content of the prior sentences within clause 6.2. As I have said earlier, the prior sentences were concerned exclusively with the guarantee provisions set out in clauses 1-4 within Schedule 6.2. They do not have the effect of creating a hybrid obligation in the sense of converting what on the face of the third sentence within the clause is a primary obligation to indemnify into a secondary guarantee obligation. The third sentence is disjunctive from the sentences that precede it. The first two sentences are concerned with the obligations set out in Schedule 6.2 while the third sentence creates a free-standing primary obligation to indemnify in respect of the categories of loss set out in it. The subheading is irrelevant because the Agreement provided that subheadings are of no legal effect – see clause 13.9 of the Agreement.

18. Finally, the nature of what is within the scope of the third sentence of clause 6.2 of itself points to it creating an indemnity because (a) it extends only to consequential losses as I have said and (b) extends to losses suffered by entities other than those to whom BML owes its obligations under the Agreement because it covers all the categories of losses identified in the sentence suffered by *" ... BFBE, BFC, and their respective Associated Companies …*" As Jefford J held in Catalyst Business Finance Limited v Very Tangy Television Limited [2018] EWHC 1669 (QB) an obligation that extends beyond losses and costs for which the principal creditor can claim will be, or is more likely to be, a primary obligation.

19. Where I part company with BFBE is in relation to its submission that as a matter of construction the third sentence of clause 6.2 makes BUKL liable to indemnify BFBE in respect of the payments that BML has refused to meet either because it has cross claims it is entitled to set off against those sums or otherwise. My reasons for reaching that conclusion are as follows.

20. First, I do not accept that any sum that is contractually due to BFBE but which is unpaid by BML is a loss that comes within the scope of the clause. Put simply, such sums are not "*... losses ... incurred in connection with any failure by BML to timely fulfil its payment obligations to BFBE and BFC under this Agreement."* Clause 6.2 distinguishes between the failure by BML to comply with its payment obligations under the Agreement (which is the subject of the guarantee obligations set out in Schedule 6.2, paragraphs 1-4 and/or the surety obligation set out in paragraph 5) and the obligation of BUKL to indemnify *" ... BFBE, BFC, and their respective Associated Companies …*" in respect of losses caused to them by BML's failure to "*... timely fulfil ... "* its payment obligations under the Agreement.

21. Secondly, construing the third sentence of clause 6.2 in this way means that full effect is given to all the language used by the parties in the whole of clause 6.2 and Schedule 6.2 and avoids construing the third sentence of clause 6.2 as covering the same ground

as that covered by paragraphs 1-4 of Schedule 6.2 and/or paragraph 5. There is no commercial logic in construing the third sentence of clause 6.2 as having the effect for which BFBE contends. Had that been intended there would have been no need for the guarantee provisions set out in paragraphs 1-4 of schedule 6.2 or the surety provision set out in paragraph 5.

22. Whilst it is true to say that in some standard form personal guarantees the words guarantee and indemnity are used together and are construed as creating both a guarantee and an indemnity, that is not what has happened here. In my judgment, the parties' intention that is apparent when the Agreement is read as a whole was to create a series of distinct obligations – the guarantee obligations at paragraphs 1 to 4 in Schedule 6.2, the surety obligation in paragraph 5 of Schedule 6.2 and the indemnity obligation set out in the third sentence of clause 6.2. Given that this was a professionally drawn agreement with both sides of the transaction advised by experienced in-house counsel, it is much more likely that each of these obligations was intended to cover different territory. It is much less likely that professional lawyers intending to cover the same or some of the same ground in each provision would separate out these provisions in the way that has been adopted.

23. The guarantee obligations are set out in paragraphs 1-4 of Schedule 6.2. As I have said already, I do not accept that the first sentence of paragraph 6.2 serves any function other than to introduce Schedule 6.2, or at least the first four paragraphs of that schedule, which contain the substantive obligations referred to in the first sentence. This is readily apparent when the first and second sentences are read together. If the first sentence was intended to have operative or substantive effect then the second sentence and Schedule 6.2 paragraphs 1-4 would be unnecessary since everything contained in paragraphs 1 to 4 would come within the scope of the first sentence. Had the intention been to create both a primary and secondary obligation in respect of the obligations within the scope of Schedule 6.2 (and additionally those within the third sentence of clause 6.2), then it would have been entirely straightforward for the lawyers acting for the parties to have created a single suite of obligations within the schedule and provide that the obligations were both primary and secondary obligations either in clause 6.2 and/or in the schedule. They did not do so. The absence of any such arrangement again suggests the intention was to cover something different in the third sentence of clause 6.2 and to do so by obligations that were different in kind from those set out in Schedule 6.2, paragraphs 1-4 and different in scope from that covered by those paragraphs and by paragraph 5.

24. Whilst I accept (as is submitted on behalf of BFBE – see T1/15/3-15) that there could be good commercial reasons in some contractual relationships for expressing a surety obligation to be both a guarantee and a primary indemnity obligation, the language used in the third sentence is obviously inapposite to achieve that purpose and is not language from which a common intention to that effect can be inferred, particularly when it is remembered that the Agreement was drafted by experienced lawyers. In this regard, if there was any residual doubt as to the effect of the language used (and in my judgment there is none) then that doubt would have to be resolved in favour of BUKL on the basis that in relation to contracts of suretyship:

> "… the courts should still in general require evidence of clear intention from the words used in a contract of guarantee to justify the nature and extent of the liability undertaken by a surety. This is also in keeping with the approach taken to contracts of

> indemnity, discussed at para.4-003. There is no justification in principle for drawing a distinction between the approach to be taken to construing contracts of guarantee and that to be applied to contracts of indemnity, particularly when there is so often such a fine line between the two types of contract"

– see Andrews & Millett, Law of Guarantees, 7th Ed., at 4-002.

25. Finally, even if I am wrong to conclude that sums due from but unpaid by BML do not come within the scope of the third sentence within Clause 6.2, I do not accept any obligation on the part of BUKL to pay has arisen because in the circumstances there has not been " … *any failure by BML to timely fulfil its payment obligations to BFBE ... under ...*" the Agreement so as to trigger BUKL's obligations as set out in that sentence. My reasons for that conclusion are as follows.

26. As I have explained, BML is relying upon a defence of equitable set off to BFBE's claim for payment. Whilst an equitable set off does not extinguish liability until agreement has been reached, or it has been determined by a judgment or an arbitral award that the cross-claims be netted off – see Stemcor UK Ltd v Global Steel Holdings [2015] EWHC 363 (Comm) *per* Hamblen J (as he then was) at paragraph 34 following earlier authority to the same effect – its effect is " … *to prevent each party from enforcing or relying on its claim to the extent of the other claim where the connection between the claims would make this manifestly unjust*" – see Gary Fearns v Anglo-Dutch Paint & Chemical Company Limited [2010] EWHC 2366 (Ch) *per* Mr George Leggatt QC (as he then was) at paragraph 26 followed by Hamblen J in Stemcor UK Ltd v Global Steel Holdings (ibid.) at paragraph 36. At paragraph 35, Hamblen J cited with approval from paragraph 18.25 of Derham on The Law of Set Off; 4th Ed. that:

> "where circumstances exist which give rise to the set-off, the creditor is not permitted in equity to assert that any moneys are due to it, or to proceed on the basis that the debtor has defaulted in payment, to the extent of the set-off. Because of the substantive nature of the defence its effect in equity is similar to a discharge of the debt pro tanto, but it does not bring about a reduction in or an extinguishment of the cross-demands at law until judgment for a set-off."

A principal debtor who has not met its obligations to its creditor because validly and in good faith it has asserted an equitable set off does not owe nor is it to be treated as having defaulted unless either it is not entitled or ceases to be entitled to validly assert the set off. In this case, BFBE cannot assert a failure on the part of BML to fulfil its payment obligations as long as BML is entitled validly to assert an equitable set off that equals or exceeds the sums BFBE claims.

27. In my judgment the expression "…*any failure by BML to timely fulfil its payment obligations to BFBE…"* means and can only mean breach of an obligation to pay. Since there is no anti-set off provision within the Agreement and it is common ground (for the purposes of these proceedings) that BML has validly asserted a defence of equitable set off that equals or exceeds the sum otherwise due to BFBE, it follows that BFBE is not permitted in equity to assert that any moneys are due to it, or to proceed on the basis that the debtor has defaulted in payment.

28. It is unreal to suppose, on the basis of the language used by the parties in the Agreement when read as a whole, that the parties at the time they entered into the Agreement intended that in such circumstances BFBE could nonetheless claim from BUKL the whole of what would otherwise be due to it, at any rate in the absence of clear wording to that effect. Had that been the intention, there is no reason why the lawyers drafting this agreement would not have inserted a no set off provision so as to preclude BML from relying on an equitable set off or inserting wording into the third sentence of clause 6.2 that made clear that BUKL's obligations under the third sentence arose notwithstanding any reliance by BML on set off or for that matter any defence. The former course would have been the most logical since in that event BML would have come under an obligation to pay notwithstanding its cross claim and the liabilities under the guarantees and indemnities would then have been triggered if BML failed to pay.

29. In summary:

    i) I accept that the third sentence of clause 6.2 creates a primary obligation; but

    ii) I do not accept that as a matter of construction it creates a primary obligation to pay sums due from BML because in my judgment the scope of this sentence is confined to indemnifying BFBE in respect of any losses as defined in the sentence incurred in connection with or which otherwise are a consequence of any failure by BML to pay; but

    iii) Even if (ii) above is wrong, the right to indemnity under the third sentence cannot arise for as long as BML is entitled validly to assert a defence of equitable set off. To suggest that it can arise is contrary to commercial sense as matters would have been perceived by reasonable people in the position of the parties, as at the date that the contract was made.

The True Meaning and Effect of Paragraph 5 of Schedule 6.2 – Issues 2, 8 and 9 in the List of Issues

30. Paragraph 5 of Schedule 6.2 provides:

> "As a separate and independent stipulation, Bacardi U.K. Limited agrees that any obligation, commitment or undertaking expressed to be undertaken by BML (including, without limitation, any moneys expressed to be payable under the Agreement) which may not be enforceable against or recoverable from BML by reason of any legal disability or incapacity on or of BML or any fact or circumstance (other than any limitation imposed by the Agreement) shall nevertheless be enforceable against and recoverable from Bacardi U.K. Limited as though the same had been incurred by Bacardi U.K. Limited and Bacardi U.K. Limited were the sole or principal obligor in respect thereof and shall be performed or paid by Bacardi U.K. Limited on demand."

31. BFBE submits that the effect of this provision is to enable BFBE to enforce against, and recover from, BUKL any obligation which BML might owe to BFBE but which might not be enforceable against or recoverable from BML other than as a result of a

contractual limitation imposed by the Agreement. BUKL describe this obligation in its submissions as "*... a limited principal debtor obligation ...*" and denies that it can be liable to BFBE for the sums BFBE claims are due from BML as a matter of construction and by reason of BML's acknowledged entitlement to rely on equitable set off as a defence to BFBE's claim for payment.

32. In my judgment this provision does not have the effect for which BFBE contends. BFBE's construction depends upon reading the words "… *by reason of ... any fact or circumstance (other than a limitation imposed by the Agreement) ...* " in isolation from the rest of the clause and, for that matter the rest of the agreement. That is a mistaken approach to the construction exercise applying the principles summarised above. In my judgment, as I have said already, the effect of this provision can only be ascertained by construing the language of the clause as a whole and in the context of the Agreement read as a whole. Looked at in that way I accept that the provision creates an obligation that is in addition to and independent of the obligations created by paragraphs 1-4 of Schedule 6.2. That is the effect of the unambiguous language used by the parties that the clause takes effect as a "… *separate and independent stipulation ...*". I also accept that the effect of the clause is that it creates a primary obligation to indemnify and that it does not take effect as a secondary guarantee obligation. That is the effect of the unambiguous language used by the parties that whatever is properly recoverable under the clause is recoverable from BUKL " … *as though the same had been incurred by Bacardi U.K. Limited and Bacardi U.K. Limited were the sole or principal obligor in respect thereof ...*". The word "*principal*" in this context means simply "primary".

33. That said, I accept as close to obvious that to " *... say that someone is primarily or secondarily liable is meaningless, since it depends on the definition of the liability in question ...*" see Carey Value Added SL v Grupo Urvasco SA [2010] EWHC 1905 (Comm), [2011] 2 All ER (Comm) 140 *per* Blair J at paragraphs 21-22. Paragraphs 1-3 within the Schedule are plainly secondary obligations for the reasons identified by Mr Graham QC in the course of his oral submissions – they are each dependent on and co-extensive with BML's obligations under the Agreement. That is not so with paragraph 5, which when read as a whole is expressly separate and independent from paragraphs 1-4 and imposes on BUKL a sole or principal obligation that is not dependent on the underlying obligations of BML being enforceable against or recoverable from BML. The liability as defined in paragraph 5 is to meet " … *any obligation, commitment or undertaking ... by BML (including, without limitation, any moneys expressed to be payable under the Agreement) which may not be enforceable against or recoverable from BML by reason of any legal disability or incapacity on or of BML or any fact or circumstance (other than any limitation imposed by the Agreement)...*". Aside from the possibility that the apparently wide scope of the words " … *any fact or circumstance ...*" may be impliedly confined by the narrower words that precede it, since if the parties' intention had been that the words were to be given their literally very wide effect there would be no need to include the words " … *any legal disability or incapacity ...*" which in consequence would be surplus, the main part of this formulation that confines its scope are the words "… *may not be enforceable against or recoverable from BML ...*". All this points firmly to the obligation being a primary indemnifying provision rather than a guarantee essentially for the reasons summarised by Mr Richard Salter QC sitting as a deputy judge of the High Court in GPP Big Field LLP and another v Solar EPC Solutions SL [2018] EWHC 2866 (Comm) at paragraph 123.

34. I now turn to the critical question, which is whether on its proper construction paragraph 5 applies in the circumstances of this case since in reality this is BUKL's main answer to the claim for payment under Paragraph 5. BUKL submits that it does not follow from BML being entitled to rely on the defence of equitable set off as a defence to the sums claimed from it by BFBE that BML's obligation to pay is or may not be enforceable or recoverable. BFBE submits that is precisely the effect of the use of the words "*not enforceable"* in paragraph 5; that they mean and were intended to mean that it became entitled to collect payment from BUKL whenever BML validly asserts a defence and that was the or one of the reasons for including the provision in Schedule 6.2. Its purpose is to enable BFBE to recover what it claims is due notwithstanding BML maintaining that it has a defence to any claims by BFBE for payment from it or for any other reason is unwilling or unable to pay. The outcome of these arguments depends on an analysis of the law relating to set off set out in part earlier in this judgment and on the construction of clause 5.

35. I return to the law relating to equitable set off referred to earlier. The effect of the defence is to " *… prevent each party from enforcing or relying on its claim to the extent of the other claim where the connection between the claims would make this manifestly unjust*" – see Fearns v Anglo-Dutch Paint & Chemical Co Ltd (ibid.) at paragraph 26. Critically, the valid assertion of the defence does not extinguish the claim to the extent of the cross claim. That occurs only when there has been a final netting off between the claim and cross claim either by agreement or a final decision of a court or arbitral tribunal – see Stemcor UK Ltd v Global Steel Holdings (ibid.) at paragraph 34. In summary therefore as between primary obligors "*[w]here a right of equitable set-off exists, the assertion of the right (reasonably and in good faith) prevents either party from enforcing its claim except in so far as its claim exceeds the value of the other. But neither claim is extinguished or reduced by the assertion of an equitable set-off. That can only be done by agreement or by judgment*" – see Woodeson v Credit Suisse (UK) Limited [2018] EWCA Civ 1103 *per* Leggatt LJ (as he then was) at paragraph 63. As I have said it is common ground for the purposes of these proceedings that BML has asserted its equitable set off defence reasonably and in good faith.

36. BUKL submits that it necessarily follows that a surety may rely on an equitable set off that has been validly relied on by a principal debtor and in support of that proposition relies on Stemcor UK Ltd v Global Steel Holdings (ibid.) at paragraph 29. To be clear, that is not the effect of that authority or any of the others relied on by BUKL at footnote 26 of its written submissions. These cases are concerned with claims against a guarantor and the proposition set out in Stemcor UK Ltd v Global Steel Holdings (ibid.) at paragraph 29 is only that a guarantor can rely on a set off in respect of an unliquidated cross-claim belonging to principal debtor. That is not disputed by BFBE. This is why it is not in dispute that the equitable set off defence asserted by BML will be available to BUKL in respect of its guarantor obligations contained in paragraphs 1 to 4 of Schedule 6.2 and the first sentence of clause 6.2 if (contrary to my view) it has any substantive effect. However it does not assist in resolving the position where, as here, the surety obligation is a primary obligation to indemnify.

37. I now return to paragraph 5. BUKL submits that the assertion by BML of a valid equitable set off defence does not render BML's obligation to pay not "… *enforceable against or recoverable from BML …"* in any relevant sense. BUKL submits that the effect of the assertion of an equitable set off defence is that it does not have that effect

because (a) the defence operates only provisionally until the claims and cross claims have been netted off by either agreement or judgment or a final award and (b) because even if ultimately netting off is ordered or is agreed, by definition that means that both the claims and cross claims will have been enforced and recovered. BFBE argues that this is wrong and that the effect of the assertion of a valid ESO is to prevent either party enforcing its claim, thus triggering BFBE's entitlement to recover what it claims to be owed from BUKL under paragraph 5. It submits that this outcome is the correct one because it makes "*... good commercial sense to give the words "not enforceable" their plain ordinary meaning. The obvious commercial purpose of the paragraph was to enable BFBE to recover the amount of the obligation from BUKL on demand and to ensure BUKL paid up if BML did not"* – see T2/43/25-44/5.

38. In my judgment, BUKL's argument is to be preferred. My reasons for reaching that conclusion are as follows. First, as a matter of construction, the words "*… enforceable against or recoverable from BML ..."* cannot be construed in a vacuum. That phrase has to be read as a whole with the rest of paragraph 5. The relevant phrase is therefore " *… enforceable against or recoverable from BML by reason of any legal disability or incapacity on or of BML or any fact or circumstance (other than any limitation imposed by the Agreement) ...*". Mr Graham does not suggest that asserting an equitable set off constitutes either a legal disability or incapacity. He submits and I think he is right about this, that this part of paragraph 5 is concerned with the effects of insolvency. It would also I think cover the example canvassed in the course of the argument of the effect of a state-imposed sanctions scheme. However, I am prepared to accept on balance and as submitted by Mr Graham at T2/46/20- 49/16 that the scope of the words " … *any fact or circumstance (other than any limitation imposed by the Agreement) ..."* are capable of extending to a wider set of circumstances than a legal disability or incapacity because the word "*or"* is disjunctive in effect.

39. However, what I do not accept is that this phrase "... *(un)enforceable against ...BML ... by reason ... of any fact or circumstance ..."* was intended to include the assertion by BML of an equitable set off defence. I say that because the effect of the assertion of an equitable set off defence by BML is not to render an obligation by BML to pay BFBE not "*… enforceable against ... BML.*". Ultimately, once the reference to arbitration of the dispute between BFBE and BML has been completed either (a) the sums claimed by BFBE will be payable by BML or (b) they won't be but only because the sums claimed by BFBE will have been netted off against the sums claimed from BFBE by BML. In either case, BFBE will have received or be entitled to receive payment in full for the sums they claim. If ultimately the outcome is as summarised in (b), that outcome could not seriously be contended to render BFBE's claims unenforceable or irrecoverable within the meaning of clause 5 so as to entitle it to payment from BUKL of the sums it had claimed notwithstanding that they had been netted off by agreement or a final award. Of course if the outcome is as described in (a) the assertion of an equitable set off defence that ultimately fails will impose a temporary cash flow impediment on BFBE. However, that does not mean that the sum claimed is irrecoverable and had the lawyers drafting this agreement intended to prevent such a cash flow difficulty, then they would have inserted a no set off provision in relation to BML's obligations or, if not for any reason (and none is suggested), they would have made clear that the paragraph 5 obligation applied in all circumstances where BML was asserting a valid defence to the sums claimed from it.

40. It is common ground as I have said that BML has validly asserted an equitable set off defence reasonably and in good faith. The effect of this is that it is also common ground that it would be "… *manifestly unjust to allow …*" BFBE to enforce payment of what it claims from BML without taking account of what BML claims it is owed by BFBE. The assertion of an equitable set off defence does not have the effect of extinguishing BFBE's claim – see Woodeson v Credit Suisse (UK) Limited (ibid.). It has the effect of not permitting BFBE in equity to assert that any moneys are due to it, or to proceed on the basis that BML has defaulted in payment, to the extent of the set-off. Critically for present purposes *" … [b]ecause of the substantive nature of the defence its effect in equity is similar to a discharge of the debt pro tanto …"* see Stemcor UK Ltd v Global Steel Holdings (ibid.) at paragraph 35, citing with approval Derham on The Law of Set Off at 18.25. In other words, the effect of the defence is to place the claimant and cross claimant, pending agreement, judgment or award, in the same position they would be in had it been agreed, adjudged or awarded that the claim and cross claim be netted off. In those circumstances BFBE's claims to payment are no more unenforceable or irrecoverable than would have been the case after such a netting off.

41. Paragraph 5 is concerned exclusively with circumstances where a sum is due to BFBE from BML either because it is indisputably due or is due by operation of a judgment or award but that sum is not enforceable against or recoverable from BML. It is not concerned with sums that are not due because they have been netted off against sums due from BFBE to BML either by agreement or judgment or award (because the effect of such an agreement, judgment or award would be to discharge the sum otherwise due from BML to BFBE) nor where BML has validly asserted an equitable set off defence reasonably and in good faith because that operates in equity in a way that is similar to discharge but does so only temporarily pending agreement, a judgment or final award determining the extent to which if at all BML is entitled to net off the sums claimed from it against the sums it claims are owed to it.

42. I reject the submission that the parties intended to enable BFBE to collect sums it claims to be entitled to recover from BML where BML has validly asserted an equitable set off defence. Once the effect of an equitable set off defence is understood to be as I have described, that is not the effect of the language used by the parties and furthermore such an outcome makes no commercial sense when viewed in the context of the Agreement when read as a whole. Had that been intended to be the outcome then the parties would have included an express no set off provision within the Agreement in relation to sums due from BML to BFBE. If the parties had intended what BFBE allege, then it is close to obvious that the way to deliver that intention is by including a no set off provision in relation to BML's obligations to pay BFBE. That would mean that BML would come under an immediate obligation to pay and if it did not the surety obligations owed by BUKL would be triggered. There is no logic in permitting BML to rely on an equitable set off but require its parent to pay what is due without regard to any equitable set off being asserted reasonably and in good faith by BML. No set off provisions are commonplace in commercial agreements and are straightforward to draft.

43. Given that the guarantees and indemnities are contained in the same document as the obligations between primary obligors, it is unreal to suppose that the intention could or would have been to permit BML to validly assert a defence or equitable set off reasonably and in good faith whilst at the same time obliging BUKL to pay any sum in respect of which a set off defence had been validly asserted by BML. This is such an

improbable commercial outcome that if it was intended very clear language would be required to achieve it. Had that been the intention and assuming that the parties had decided not to impose a no set off provision on BML, it was open to the parties to achieve that result by simply including a no set off provision either within clause 6.2 or in a generally applicable clause within schedule 6.2 or by an additional sentence in clause 5. The parties chose to do none of these things.

44. In summary clause 5 of Schedule 6.2 is of no application. The sums BFBE claims to be due from BML are not irrecoverable from or unenforceable against BML in the sense intended by the parties by clause 5 of the schedule. Had it been intended that any sums due to BFBE from BML in respect of which BML validly claimed an equitable set off should nonetheless be recovered in full from BUKL, then plain words were required and they have not been used. Further, the absence of a no set off provision as between BML and BFBE is inconsistent with that being the intention. Although it is submitted by BFBE that the construction for which it contends makes "*... good commercial sense ...*" that is only arguably so from BFBE's perspective. In this case as with many others which depend on construction, either outcome is capable of making commercial sense. That is why in arriving at a result it is necessary to consider the provision relied on in its true commercial context, which involves considering the position as between BML and BFBE as well as between BUKL and BFBE.

The Effect of the Rule in Holme v Brunskill – Issues 4, 5, 6 and 7

45. BUKL's case is that the result of the AA is that BUKL was discharged from each of its surety obligations under the Agreement, pursuant to the rule in Holme v Brunskill.

46. The effect of the rule is well known - any material variation of the terms of the contract between the creditor and the principal creditor will discharge the surety. Where a variation has occurred, the creditor must show that the nature of the alteration can only be beneficial to the surety or that by its nature it cannot in any circumstances increase the surety's risk.

47. An initial point of law that arises concerns the applicability of the rule to indemnities as opposed to guarantees. This issue was most recently considered by Mr Richard Salter QC sitting as a deputy judge of the High Court in GPP Big Field LLP and another v Solar EPC Solutions SL [2018] EWHC 2866 (Comm). An issue in that case was whether a provision was an indemnity in the sense referred to earlier in this judgment or a guarantee again in the sense referred to earlier. Having concluded that the relevant provision was an indemnity, the Judge then considered whether the rule I am now considering applied to indemnities or only to guarantees. Having carried out a comprehensive review of the relevant authorities starting at paragraph 131, he set out his conclusions at paragraph 145-147 in these terms:

> "145. Drawing these various threads together, it seems to me that the overwhelming preponderance of view in the cases and textbooks which have been cited to me is that the rule in Holme v Brunskill does not apply to contracts of indemnity, properly so called. …
>
> 146. In my judgment, the correct course for me as a first instance judge is to follow the trend of the dicta, assumptions and

> decisions in these more modern cases, and to hold that the equitable protections relied on by Solar in the present case apply only to contracts that are properly characterised as contracts of guarantee, and do not apply to contracts of indemnity, any more than they apply to on-demand bonds or to standby letters of credit.
>
> 147. There are, in my judgment, sound reasons of policy to support that conclusion, and for not extending the ambit of the rule in Holme v Brunskill beyond that established by binding authority. It is generally acknowledged that the rule in Holme v Brunskill unduly favours the guarantor, in that it discharges the guarantee completely upon the occurrence of any variation which is not "obviously unsubstantial" or clearly for the benefit of the guarantor. It represents a trap for the unwary creditor. Yet it is plainly not regarded as a fundamental right of the guarantor, since the law (subject to any relevant statutory control of unfair terms) permits the creditor to contract out of it by the terms of the guarantee. All well-advised creditors therefore do so: but that, in turn, leads to the uncertainties of the "purview doctrine" which, in reliance on the historical origins of the rule, limits the extent to which such clauses can be effective. Declining to extend the ambit of the rule in Holme v Brunskill to contracts of indemnity, properly so called, therefore promotes legal certainty."

These views were endorsed in O'Donovan, The Modern Contract of Guarantee; 4th ed at paragraph 7-070 and reflects the approach adopted by Flaux J as he then was in ABN Amro Commercial Finance Plc v McGinn [2014] EWHC 1674 (Comm) at paragraph 37 where he concluded that " … *on the true construction of the deeds of indemnity, the defendants' liability in each case is primary, so that the defence based upon the rule in Holme v Brunskill is not available to the defendants …*".

48. In light of this material, I accept BFBE's submission that the rule in Holme v Brunskill does not apply either to the indemnity obligation set out in the third sentence of clause 6.2 or to the obligation under paragraph 5 of Schedule 6.2. I reach this conclusion because it would be wrong for me to differ from the conclusions on issues of law of judges of coordinate jurisdiction unless I was satisfied that those conclusions were plainly wrong. I am not so satisfied. On the contrary, I consider these conclusions to be correct. In particular, I respectfully adopt Mr Salter's analysis at paragraph 147 of his judgment quoted above – the rule unduly favours guarantors for all the reasons he identifies; it represents a trap for the unwary and as Dr Courtney argues convincingly in O'Donovan at paragraph 7-073, it merits reconsideration. It is certainly not appropriate to extent the scope of the rule beyond its current parameters.

49. I reject the submission made on behalf of BUKL that the applicability of this rule depends on whether the relevant instrument, when read as a whole, contains only an indemnity or indemnities in the sense described earlier and does not or may not apply where the instrument contains a mixture of guarantees and indemnities. There is no justification for such an approach to be found in the authorities in the circumstances of this case, where the only operative provision within clause 6.2 is the indemnity

provision in the third sentence and where the surety provisions within Schedule 6.2 are set out in separate and distinct paragraphs. In my judgment, it is necessary to decide whether the surety obligation is a primary or secondary guarantee obligation in each case and by reference to each distinct obligation. The rule I am now considering applies only to obligations falling into the second of these categories. Adopting the approach contended for by BUKL involves extending the scope of a rule that is flawed for the reasons I have summarised above. There is no justification for adopting such an approach.

50. These conclusions mean that Issue 7 must be resolved in favour of BFBE.

51. Issue 6 is concerned with the impact of the rule on the pure guarantee obligations. As such the only issues that arise concern consent and materiality.

52. I turn first to the consent issue. As Mr Salter QC held in GPP Big Field LLP and another v Solar EPC Solutions SL (ibid.) at paragraph 173, " … *the rule in Holme v Brunskill exists for the protection of guarantors, not for the protection of creditors: and the law is clear that mere knowledge of a proposed variation on the part of a guarantor is not the same as his consent to it. It follows that the consent of the surety must generally be communicated to the creditor in order to be effective* …". It is common ground however that consent may be inferred from the circumstances. Where an individual guarantor agrees to a variation of the agreement containing the guaranteed obligations between the creditor and a corporate principal debtor of which he is a director, a court will readily infer consent by the director concerned in his or her personal capacity as guarantor from his or her agreement to the variation in his or her capacity as director of the principal debtor – see by way of example Beck Interiors Limited v Russo [2009] EWHC 3861 (QB) *per* Ramsay J at paragraph 34 and Moat Financial Services v Wilkinson [2005] EWCA Civ 1253 *per* Neuberger LJ (as he then was) at paragraphs 14 – 15 where he rejected an argument to the contrary as flying in the face of reality. It remains the case however that the presence of consent is an issue of fact that depends on the evidence available in each case. Mr Graham submits that the effect of these authorities in summary is to demonstrate that the court is unwilling to allow separate legal capacities to negative consent and that therefore express consent to the variation in one capacity will be implied consent in other capacities for the purposes of the rule in Holme v Brunskill – see T2/123/20-24.

53. Had BUKL been an individual guarantor and had that individual signed the AA on behalf of BML, I would have had little difficulty in concluding that in the circumstances consent to the variation on behalf of BML would have been implied consent by the individual for the purposes of the rule. However, it is submitted on behalf of BUKL that since it is a company and since the AA has not been executed by anyone on behalf of BUKL it follows that it cannot be inferred that BUKL has consented to the variation even though, as is common ground, the AA was executed on behalf of BML by two of its directors who were also directors of BUKL. Mr Graham submits that this is not a sound basis for distinguishing the authorities he relies on, even though none of the authorities he has cited concern a corporate as opposed to an individual guarantor. He submits that the principle of law to be derived from the authorities he relies on including the two I refer to above is that I should consider as a matter of fact whether the guarantor has consented and I should not be concerned about artificial and unrealistic distinctions as to formal legal capacity and that the principle applies equally to natural and legal

persons and that to decide otherwise is an artificial and unreal distinction that "... *flies in the face of reality and should be rejected"* – see T2/125/6-24.

54. Mr Davies-Jones QC submits on behalf of BUKL that where consent is alleged to have been given on behalf of a company different considerations apply, that nothing short of written consent on behalf of BUKL will do and that consent cannot be inferred. I reject that submission. If and to the extent reliance is placed on the fact that BUKL signed the Agreement for the purpose of agreeing to be " … *bound by the obligations and undertakings set forth in section 6.2 (Parent Guarantee) and agrees to execute the Guarantee in the form attached as Schedule 6.2*." that is immaterial. That was a formal requirement in order to comply with the Statute of Frauds in relation to contracts of guarantee provisions within the Agreement. Consent in the context I am now considering does not require any such formal agreement.

55. In my judgment where the facts permit it, consent in this context may be inferred on behalf of a company just as it can be inferred on behalf of an individual but subject to the requirement that a company can only act by an agent that is actually or ostensibly authorised to act on behalf of the company concerned. Although concerned with consent by a local authority rather than a company, in my judgment the reasoning on this issue in Credit Suisse v Allerdale BC [1995] 1 Lloyd's Rep 315 applies because the distinction between a company and a statutory authority is a distinction without a difference.

56. That case was concerned with a loan to a company controlled by the Council that had been guaranteed by the Council by an all-monies guarantee. The issue in that case was whether the Council had consented to a variation to the facility given to the company. The variation had been negotiated by the solicitor to the Council on the instructions of the chief executive and it had been approved by the board of the company consisting of four councillors and the Council's chief executive. On this basis Colman J concluded that there could be no doubt that the Council had knowledge of the variation but then the Judge asked himself whether the Council had consented. This approach accords with the authorities cited earlier in this judgment to the effect that knowledge does not necessarily equate to consent. The judge found that the officers of the Council had actual authority to consent and that when the Council's solicitor on instructions from the Council's chief executive returned to the bank on behalf of the company a letter on Council letterhead confirming consent to the revised facility he consented on behalf of the Council as well as the company. The Judge added that it had been argued that even if the case on actual authority was wrong the officials nevertheless had ostensible authority to consent. The Judge said there was no need for him to decide that point and he did not.

57. In my judgment it is plain from this authority and in any event is obvious that before an individual can consent on behalf of a company or statutory body that individual must have either actual or ostensible authority to give such consent. The sole issue on consent therefore in the circumstances of this case is whether the directors who executed the AA on behalf of BML had either actual or implied actual authority or ostensible authority to provide consent as required by the rule in Holme v Brunskill.

58. Mr Davies-Jones submits that the effect of this authority is to require a written representation embodying the relevant consent. With respect this authority does not say any such thing. In my judgment once it is concluded that the individual signing or

otherwise approving the relevant change on behalf of the principal debtor also had ostensible or implied actual authority to provide consent on behalf of a corporate guarantor then the court will approach the question of whether consent has been given in the same way that the issue was approached in cases concerning individual guarantors illustrated by authorities such as Beck Interiors Limited v Russo (ibid.) and Moat Financial Services v Wilkinson (ibid.).

59. The evidence concerning authority that is available has gone unchallenged. The evidence of Ms Almond (one of the two signatories of the AA on behalf of BML and a director of both BML and BUKL) on this issue is:

> "As noted above, I cannot recall ever having done anything for BUKL outside of a board meeting. The Addendum Agreement was never discussed in a BUKL board meeting, or otherwise considered by me as a BUKL director outside of a board meeting, either prior to or following its execution. No-one sought BUKL's consent to the Addendum Agreement and BUKL never considered giving it. Nor did it authorise BML to enter into the Addendum Agreement on its behalf (which I am told is part of the case being advanced by BFBE). If I had thought at the time of signing the Addendum Agreement about whether I was signing on behalf of BUKL (which I did not), I would have concluded that I was not and that I was only signing on behalf of BML."

The evidence of Mr Bilsland (the other signatory and director of both companies) on this issue is that:

> "There was no BUKL Board Meeting at which the Addendum Agreement was discussed and no resolution of the Board considering it in any way, or otherwise authorising or consenting to it. At the time of signing the Addendum Agreement I had been a director of both companies (BUKL and BML) for a little over 9 months. In that time my only actions on behalf of BUKL had been to attend two short board meetings. The first was to appoint me as a director. The second was to approve BUKL's accounts and approve a dividend. On neither occasion was any other business transacted. I do not do anything for BUKL outside of the formal board meetings, and I have never been required to do so. All of my actions set out above which related to the Addendum Agreement were undertaken by me in my role as BML's Finance Director."

The fact that neither Mr Bilsland nor Ms Almond considered themselves to be acting for BUKL is of itself immaterial. It is also noteworthy that Ms Almond does not say that she lacked implied actual or ostensible authority to give consent but only that BUKL did not authorise BML to act on its behalf. Mr Bilsland does not address the authority issue directly. Nonetheless I accept Mr Davies-Jones's submission that on this evidence I cannot find that either Ms Almond or Mr Bilsland had actual authority to consent to the changes effected by the AA on behalf of BUKL. However that says

nothing about whether they had implied actual or ostensible authority to consent on behalf of BUKL.

60. Mr Davies-Jones submits that it is not open to BFBE to argue that Ms Almond and/or Mr Bilsland had implied actual or ostensible authority to provide consent on behalf of BUKL because that allegation has not been pleaded.

61. BFBE's pleaded case as to consent is set out in paragraphs 10.4 to 10.6 of its amended Reply in these terms:

> "10.4. Clause 4 of the Addendum Agreement provided, in relevant part, as follows:
>
> > "*Each of the parties agrees that it has received adequate and independent consideration for entering into this Addendum Agreement on behalf of itself and its Associated Companies*";
>
> 10.5. The Defendant was one of BML's Associated Companies (as defined in the Agreement);
>
> 10.6. In the circumstances BML entered into the Addendum Agreement on its own behalf and on behalf of its Associated Companies and BML's consent to the terms of that agreement also constituted the consent of the Defendant to those terms. Alternatively, the Defendant's consent to the terms of the Addendum Agreement can and should be inferred from the terms of the Addendum Agreement, including but not limited to the terms of the Addendum Agreement referred to above;"

It is true to say that it is not anywhere alleged that the directors of BML who signed the AA had actual, implied actual or ostensible authority to consent on behalf of BUKL. Even if it could be anticipated that BFBE would rely on the appointment of Ms Almond and Mr Bilsland as directors of BUKL as a sufficient holding out of them by BUKL as having authority to act on behalf of BUKL, that does not address the other elements of a case based on ostensible authority and in particular who on behalf of BFBE relied on the implied consent supposedly given by Ms Almond and Mr Bilsland on behalf of BUKL. No evidence on this issue has been adduced by BFBE.

62. On this basis – the lack of a pleaded case going to this issue coupled with no evidence being adduced by BFBE going to this issue – BUKL is fully entitled to maintain that it has been taken by surprise and so should not be required to meet a case that it has had no notice of. Mr Graham's response to this submission was in essence that it was legalistic technicality devoid of any practical or commercial reality. He added that his case is and always was that pleaded in paragraph 10.6 of the Amended Reply – that consent can and should be inferred from execution of the AA. However that misses the point almost entirely, which is that neither BML or those acting on its behalf could provide consent on behalf of BUKL unless they had either actual, implied actual or ostensible authority to do so. That issue is not addressed in the Reply nor in any evidence served on behalf of BFBE.

63. Although Mr Graham suggested that the answer to these issues lies in the List of Issues that is not so. I agree that if the List of Issues had identified the issue I am now considering as one that had to be resolved at this trial, it would have been more difficult and perhaps impossible for BUKL to complain that it had been taken by surprise by BFBE's attempts to assert that Ms Almond and Mr Bilsland had ostensible authority to give consent on behalf of BUKE but that is not the position. The only material issue for present purposes is Issue 5 ("Did BUKL consent to the terms of the Addendum Agreement"). That formulation simply begs the issue. In the end, although Mr Graham dismisses this issue as "*… a technical legal point rather than a simple point based on the facts …*" – see T4/88/3-4 – it is much more than that. The point is fundamental to how artificial entities with their own legal personalities such as companies and independent statutory authorities can act in any given situation. It is not a point that can simply be ignored on the basis that it is inconvenient. Mr Graham's attempt to distinguish Credit Suisse (ibid.) on the basis that it concerned an independent statutory authority rather than a company does not assist either. In both cases, the entity can only act by actually or ostensibly authorised agents.

64. In those circumstances, I resolve Issue 5 by concluding that BUKL has not been proved by BFBE to have consented to the variations contained in the AA.

65. I now turn to materiality, which is the subject of Issue 4.

66. At one level this issue concerns a significant amount of detail concerning an internal reorganisation which at least in part I will have to comment upon. However in my judgment much of the detail is immaterial because of the strict nature of the test of materiality that the case law establishes for present purposes. In Holme v Brunskill itself, the nature of the enquiry was described as being a strict one:

> " … although in cases where it is without inquiry evident that the alteration was unsubstantial, or that it cannot be otherwise than beneficial to the surety, the surety may not be discharged; yet, if it is not self-evident that the alteration is unsubstantial, or one which cannot be prejudicial to the surety, the Court will not, in an action against the surety, go into an inquiry as to the effect of the alteration or allow the question, whether the surety is discharged or not, to be determined by the finding of a jury as to the materiality of the alteration or on the question whether it is to the prejudice of the surety …"

The English courts have constantly maintained this very strict approach – see by way of example Barclays Bank plc v Kingston [2006] EWHC 533 (QB); [2006] 1 All ER (Comm) 519 *per* Stanley Burnton J at paragraph 15; National Merchant Buying Soc Ltd v Bellamy [2013] EWCA Civ 452; [2013] 2 All ER (Comm) 674 *per* Rimer LJ at paragraph 30 and Credit Suisse v Allerdale BC (ibid.) *per* Colman J at 365-366. Mr Graham's reliance on Raiffeisen Zentralbank Osterreich AG v Crossseas Shipping Ltd [2000] 1 WLR 1135 is mistaken because that case is not concerned with the application of the rule in Holme v Brunskill. As the applicable principle is summarised in the current edition of Chitty on Contracts 33rd Ed., at paragraph 45-104,

> "It is immaterial that the variation has not in fact prejudiced the surety, or that the likelihood that it may do so is remote. … The

> principle is applied very strictly so that even the most trifling variation may discharge the surety."

The onus rests on BFBE to show that the changes made by the AA were immaterial applying these principles – see Topland Portfolio No.1 Ltd v Smiths News Trading Ltd [2014] EWCA Civ 18, [2014] 1 P&CR 17 *per* Arnold J (as he then was) at paragraph 20.

67. The genesis of the AA was an internal reorganisation within the group of which BML and BUKL were at all material times a part. The effect of these changes was that services hitherto provided by "*Hub personnel*" as defined in Schedule 6.1 of the Agreement would be provided by "*Region Personnel*" and it was agreed that BFBE would reimburse BML with a proportion of "*Overhead Costs*" relating to the Region Personnel as defined in the table in clause 1(a) (b) of the AA with all other costs relating to the BML Services continuing to be re-charged to BFBE as provided for in the Agreement. BFBE maintained at trial that the operative provisions within the AA had already been agreed a year prior to the date of the AA and that the AA merely gave effect to what had been agreed under the terms of the Agreement itself and so did not prejudice BUKL's position.

68. BUKL maintains that this assertion should be rejected for a number of reasons. First, it is submitted (as was common ground) that the Agreement could not be varied other than in writing executed by all parties affected. I accept this submission. Indeed it was not and could not be disputed given the terms of clause 13.8 of the Agreement. It follows that either (a) the Agreement did not require amendment at all in which case the AA was unnecessary and therefore immaterial or (b) it was required in order to give legal effect to what had been agreed prior to its execution. I accept BUKL's submission that the latter is the correct analysis. Schedule 6.1 of the Agreement defined "*Hub Personnel*" and provided for BFBE to pay a proportion of the "*Hub Personnel Costs*". It was submitted by BUKL that following the reorganisation that swept away the "*Hub*" structure and replaced it with a regional personnel structure, BML would no longer be entitled to recover a costs contribution under the Agreement because the structures referred to in the Agreement would cease to exist following the reorganisation. I accept that submission and I accept also that if a contribution to costs was to be formalised it required an amendment of the Agreement so that it reflected the new Bacardi operating structure. It may well be the fact that a pragmatic commercial arrangement had been arrived at prior to execution of the AA but it was not one sanctioned by the Agreement for the reasons identified by Mr Davies-Jones. Mr Graham relies on an internal memorandum from Bacardi's Legal Director of Northern Europe recording her reasoning for why a variation was required as being that "*We are already back dating these changes to April 2018, and I'm sure auditors will want to see signed agreements recognising the changes to the Hub costs on both sides* ...". This does not assist BFBE. The key point about this reasoning is that the auditors would require such an agreement because without it there was no formal legal basis for the arrangements that had been made because they could not be justified by reference to the existing terms of the Agreement.

69. BUKL submits that the effect of these changes was at least potentially to reduce BFBE's contributions in real terms and therefore increase the sums payable to BFBE by BML and so potentially increase BUKL's exposure under its guarantees and indemnities because they replaced the right to a contribution to Hub Personnel Costs with a right to

charge a fixed proportion of the cost of providing a smaller group of staff. That this is so is apparent by comparing the 13 employees identified as constituting "Hub Personnel" in Schedule 6.1 of the Agreement with the list of regional personnel in Clause 2(a)(b) of the AA. As Mr Davies-Jones submits, "*… the variation therefore had the capacity to reduce the cost contribution payable by BFBE and/or increase the revenue to be remitted. That, in turn, had the capacity to increase the sums due to be paid by BML to BFBE under the Agreement. That, in turn, had the capacity to increase BUKL's potential liability to BFBE as surety to BML..*.". He submits that the enquiry on this issue ends there because the AA was clearly capable of prejudicing BUKL's interests and "*… the Court will not, in an action against the surety, go into an inquiry as to the effect of the alteration …*".

70. Mr Graham submits that even applying the strict approach referred to above, BUKL cannot prove even a potential adverse effect. Mr Graham submits that:

> "…the key point here is that BML's payment obligations were variable in nature and that they depended upon both BF products, the volume of BF products sold each month, and the budget agreed between the Parties in each year. That was the obligation my Lord that was guaranteed by BUKL, not a fixed payment but a variable one dependent upon factors outside the control of the Parties and also on the parties' own budget agreement"

and that the variation of the Agreement by the AA simply gave effect to what had commenced in April 2018 because the Parties had reached a commercial agreement on that point through the process of agreeing the budget for the year, for the financial year 2019. This ignores the fact that what had been agreed commercially was not possible under the Agreement unless it was varied, the Agreement could not be varied otherwise than in writing and if the commercial arrangement took effect as an informal variation of the Agreement then that as much engages the rule in Holme v Brunskill as does the AA. It also ignores the fact that the level of detail implicit in these submissions ignores the requirement that the court should not enquire into the effect of a variation.

71. In relation to potential effect, Mr Graham submitted that the AA could not prejudice BUKL because it made no difference since it was simply "*... a formal acknowledgement of what the parties were already doing ...".* Pausing there, that does not provide an answer unless what they were doing was permitted by the Agreement in its unamended form. That was what Mr Graham submitted was the position but it was not – if that had been the case there would have been no need to vary the terms of the Agreement whether to satisfy auditors or at all. Mr Graham returned to this theme in his reply submissions. Given Mr Davies-Jones' submissions (which in this regard reflected what had been set out in his written submissions) the following exchange took place:

> "HIS HONOUR JUDGE PELLING: What about the point that it reduced the number of personnel in respect of which recharge could apply, thereby reducing the amount of recharge, thereby increasing the potential exposure of the guarantor, or indemnor, as the case may be?

> MR GRAHAM: I think two points on that. Firstly, that a reduction in the numbers does not necessarily mean that those remaining will be paid the same amount. So there is obviously ––there was latitude on the Parties within the budget to agree that the relevant back office functions at a pretty senior level can be dealt with by a smaller number of more senior people or a greater number of more junior people. That does not alter the fact that making that sort of change has already been agreed. That is part of the exposure that has already been agreed to under the contract. What is changing is the label. So if one decided to introduce fewer but more senior people at the hub level, you have not changed the label "hub personnel", that would be fine, and that is indeed what happened in finance year 2019. One is assuming that it was not open to the Parties to introduce a greater number of personnel at higher expense, smaller personnel at greater or lesser expense, all of that was open to the Parties as part of the variable budgeting arrangements to which they had already signed up. What BUKL was guaranteeing was BML's payment obligations, among other things, under that schedule. The Parties wouldn't have agreed that they could make their agreement unless it was simply a question of labelling. They knew it was open to them to make the budget agreement, which they made and did make and operated, within the confines of the existing agreement. So therefore treating all the new personnel not as region personnel but as hub personnel for the time being.
>
> All that changes, when the agreement comes into effect, is the labelling, so we say the actual substantive change is made in the budget agreement which was in the scope of the original unamended Cost Sharing Agreement. In our respectful submission the variation affected by the addendum agreement was as to labelling only and therefore not material. My Lord that was all I was proposing to say on the fifth topic."

As to these points, they are entirely speculative amounting as they do to an assertion that the cost may be the same. That is mistaken firstly because it does not address the test that has to be applied following the authorities referred to earlier. Secondly, it ignores the fact that if the variation was to be shown to be immaterial, it was for BFBE to prove it. This submission does not achieve that objective. Thirdly, it ignores the requirement not to enquire into the effect of the variation but to enquire only if either (a) it could only benefit the surety or (b) cannot in any circumstances increase the surety's risk. These submissions do not answer Mr Davies-Jones' point or satisfy that test. On any view the changes that have been affected by the AA are in my judgment ones where it has not been shown self-evidently to benefit or not prejudice the surety.

72. These conclusions mean that Issue 4 and Issue 6 must be resolved in favour of BUKL.

73. I will hear the parties after hand down of this judgment as to the form of order required to carry these conclusions into effect.