DOUBLE JEOPARDY: BREACH OF SANCTION

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The case of Lamesa Investments Ltd v Cynergy Bank Ltd [2019] EWHC 1877 (Comm) involved a bank caught up in the crosshairs of international sanctions but could apply to any contractual scenario.

The Facts

Lamesa was a company registered in Cyprus, ultimately owned by Viktor Vekselberg.

Cynergy was a UK retail bank with a US Dollar correspondent account with a US bank.

Lamesa advanced £30 million to Cynergy, with interest payments due every six months.

There was a clause in the loan agreement that provided:

"[Cynergy] shall not be in default if…such sums were not paid in order to comply with any mandatory provision of law, regulation or order of any court of competent jurisdiction."

Sanctions

In April 2018, Mr Vekselberg was placed on a list of 'Specially Designated Nationals' (SDN) by the U.S. Department of the Treasury's Office of Foreign Assets Control (OFAC). As a result, Lamesa became a 'blocked person'.

This meant that any US person anywhere in the world, any person dealing with property subject to US jurisdiction or any person operating in the US is potentially subject to 'primary sanctions' if they deal with Mr. Vekselberg, as a SDN, or Lamesa, as a blocked person.

However, 'secondary sanctions' also apply to non-US persons with no property or operational connection to the US in relation to a SDN or blocked person, in particular, on foreign financial institutions that knowingly facilitate 'significant' financial transactions on behalf of a blocked person.

There was no dispute that if Cynergy's payment of interest to Lamesa was a 'significant financial transaction', the US Government had the power to impose secondary sanctions on Cynergy and such a sanction would be highly damaging to Cynergy's business.

Cynergy was in an unenviable position of having to choose to comply with its contractual obligation to pay interest or face sanctions. Cynergy withheld £3.6 million in interest citing the exclusion clause in the loan agreement referred to above.

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Legal claim

Lamesa sought a declaration in the UK High Court to the effect that the exclusion clause did not entitle Cynergy to avoid payment and that the outstanding interest was due and payable.

Cynergy argued that in light of the risk of secondary sanctions on it, this was a 'mandatory provision of law'. Therefore its non-payment of the interest was within the scope of the exclusion clause.

Lamesa sought to argue that the risk of secondary sanction was not an express prohibition and that 'mandatory' should mean 'compulsory'. It also argued that 'provision of law' in the context of the agreement meant English law. The exclusion clause did not apply in the circumstances.

Legal analysis

Under English common law, contractual performance of an English law contract by reason of supervening illegality is excusable in limited circumstances:

- if it is illegal to perform it under English law; or
- if it is illegal under the law of the place where the contract is to be performed

neither of which applied in this case.

However, earlier cases (including National Bank of Kazakhstan v Bank of New York Mellon [2018] EWCA Civ 1390) have confirmed that the common law position can be reversed by express agreement. The English Court can determine whether the parties intended the exclusion clause to cover the potential imposition of US secondary sanctions and thereby reverse the common law position in this case.

Lessons of Lamesa

1. A 'mandatory provision of law' simply meant a law that could not be derogated from, i.e. one that could not be waived by agreement of the parties.
2. The exclusion clause referred to 'any court of competent jurisdiction' and the definition of 'regulation' was also very wide: 'any regulation, rule, official direction, request or guideline [...] of any governmental [...] agency or of any regulatory [...] organisation'. There was no territorial qualification in the clause. Hence there was no basis to limit the application of this clause to English laws only.
3. Common law provides limited protection against sanctions risk, or any other 'double jeopardy' risk, where cross-boder liabilities might arise.
4. This risk can be mitigated by clear drafting, adopting language which is wide enough to cover a multitude of eventualities which constantly evolve.

The judgment in Lamesa provides comfort to financial institutions seeking to manage, contractually, their exposure to the global reach

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of sanctions.

Whilst this is an English case applying English law principles, the parallels are clear. If a similar situation arose in Guernsey involving a Guernsey institution with international customers, undertaking activities which may be subject to sanctions or other laws, the ruling in Lamesa would likely be relevant.

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