



Corporate Turnaround and Insolvency

Conditions for granting relief against forfeiture of shares

The case of *Cukurova Finance International Limited and another v Alfa Telecom Turkey Limited [2013]* provides interesting guidance on the basis upon which a court will grant relief from forfeiture in respect of charged shares in circumstances where repayment had been proffered, and the level of compensation (in terms of interest) that a borrower may be required to pay to a lender should relief from forfeiture be granted and the charged property returned.

Background

Alpha Telecom Turkey Limited ('ATT') lent the respondent ('CFI') US\$1.352 billion secured by share charges over shares in one of its BVI subsidiaries ('CTH') and over the shares in CFI held by its parent company ('CH'). CFI later defaulted under the facility agreement allowing ATT to appropriate the shares secured under the share charge. Within a month of the default, CFI offered to repay the loan in full, but ATT rejected the repayment arguing it was too late because ATT had exercised its right to accelerate the facility and was therefore entitled to appropriate the charged shares in full or partial discharge of the loan, which it had duly done.

CFI and CH started proceedings seeking an order requiring ATT to accept the repayment of the loan and the redemption of the security. The redemption monies were held in an interest bearing escrow account throughout

The outcome

The Privy Council decided that an event of default had been established by ATT and ATT's appropriation of the shares had not been tainted by bad faith or an improper purpose (i.e. the intention of obtaining control of the subsidiary Turkcell, a Turkish mobile phone network provider, which would have given ATT effective control of the Turkish telecoms industry). The Privy Council ruled however that relief from forfeiture should be available to CFI and CH on condition that CFI and CH pay to ATT the redemption sum, interest on the redemption sum accruing between the date of the judgment and the date of payment of the redemption sum, and an amount on account of costs on the standard rather than indemnity basis. This was on the basis that it would be inequitable to treat the loan as still outstanding for the period after appropriation in circumstances

where repayment had been tendered and specifically set aside for allocation against the debt.

Interestingly the Privy Council was divided as to the reasoning behind the decision.

Reasoning of the Privy Council

The main issue that divided the Privy Council was whether relief was to be granted on the basis that the loan was to be treated as having remained unpaid from the date of appropriation of the shares (in which case more interest to the date of the court order would be payable) or whether the circumstances of the case allowed for discretion to adopt a different approach. The minority argued that the loan had not been satisfied by the appropriation of shares, and that the contractual terms of the loan agreement should govern the redemption sum payable by CFI. The majority accepted that in normal circumstances relief in equity would only be granted on the basis of conditions requiring performance in accordance with the terms of the relevant contract, but that this was a not entirely inflexible rule. They argued that in exceptional situations such as this, there may be circumstances that make it inequitable or unconscionable to insist on treating the loan as if it had remained continuously outstanding until the court order was made. The majority therefore reached the conclusion that the appropriation had discharged the loan.

This, for reasons explored below, is somewhat odd reasoning, however the fact that CFI and CH had offered to repay the loan and had actually set the redemption monies aside were directly relevant to the decision by the majority. The Privy Council ruled that it would be inequitable and unconscionable to ignore the fact that CFI and CH had offered to redeem the loan, and to treat the grant of relief as conditional on the loan remaining outstanding as if nothing had happened in the meantime. ATT had rejected the opportunity to receive payment in full and the tender of repayment by CFI, together with the redemption monies being kept in an escrow account, prevented interest running subsequently when assessing what CFI had to pay to redeem its shares. The effect of the court order effectively extended the repayment date under the loan agreement.

The future

Although the Privy Council's decisions are not technically binding on courts in England and Wales, they are considered persuasive authority. The different views of the Council in this case do leave an element of uncertainty as to which view English courts would take. If the reasoning of the majority is followed, then lenders cannot be certain that the appropriation of shares (and other forms of financial collateral) under the Financial Collateral Arrangements (No.2) Regulations 2003 will directly repay or reduce the amount of a loan and extinguish the borrower's "equity of redemption" to its security (which is precisely what the Regulations look to achieve). Although admittedly the case, according to the majority view of the Privy Council, was exceptional due to the unusual circumstances (the commercial interests of the case, the subsequent tendering of payment and the lenders' refusal to accept that payment being chief amongst them), it may be that other borrowers will argue that their circumstances are equally exceptional.

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