

Singapore Management University

## Institutional Knowledge at Singapore Management University

---

Research Collection Yong Pung How School Of Law

Yong Pung How School of Law

---

9-2022

### Novation and advance consent

Kwan Ho LAU

Singapore Management University, [kwanholau@smu.edu.sg](mailto:kwanholau@smu.edu.sg)

Follow this and additional works at: [https://ink.library.smu.edu.sg/sol\\_research](https://ink.library.smu.edu.sg/sol_research)



Part of the [Commercial Law Commons](#), and the [Contracts Commons](#)

---


#### Citation

LAU, Kwan Ho. Novation and advance consent. (2022). *Cambridge Law Journal*. 81, (3), 581-609.

Available at: [https://ink.library.smu.edu.sg/sol\\_research/3979](https://ink.library.smu.edu.sg/sol_research/3979)

This Journal Article is brought to you for free and open access by the Yong Pung How School of Law at Institutional Knowledge at Singapore Management University. It has been accepted for inclusion in Research Collection Yong Pung How School Of Law by an authorized administrator of Institutional Knowledge at Singapore Management University. For more information, please email [cherylds@smu.edu.sg](mailto:cherylds@smu.edu.sg).

## NOVATION AND ADVANCE CONSENT

KWAN HO LAU\* 

**ABSTRACT.** *Professor Goode once observed that “Novation need not be left to ad hoc agreement; it is open to the parties to provide for it in advance and in particular to establish a contractual mechanism by which novation takes place automatically on the occurrence of a designated act or event”. This deceptively straightforward proposition is examined in the present article. It explores the legal footing for, and the risks in adopting a pristine version of, the proposition, and considers possible safeguards that may be incorporated within the process of scrutiny, if in any case there arises concern over the effectiveness of a novation that is undertaken pursuant to consent given in advance.*

**KEYWORDS:** *contract, novation, commercial law, common law.*

### I. INTRODUCTION

For a time the law of assignment and novation seemed harmonious and complete. It generally reflected and promoted commercial practices, and there were rules that were clearly directive, if overly categorical on occasion. But lately it has taken on a resemblance to the proverbial duck. Despite carrying necessary adaptations to suit modern-day commerce, the underlying theoretical discipline has been paddling furiously to keep it afloat.<sup>1</sup>

The purpose of this article is to examine one of those deceptively comfortable positions. Writing in 1995, Professor Roy Goode Q.C. observed

\* Assistant Professor of Law, Singapore Management University. Much of this article was written while holding the DS Lee Foundation Fellowship. Earlier drafts were presented at the Society of Legal Scholars Annual Conference 2019 (University of Central Lancashire), Contracts Conference 2019 (Melbourne Law School) and Asia-Pacific Private Law Conference 2021 (University of Hong Kong). I am grateful for the feedback received at those forums. Especial thanks are due to Felicity Maher, James Penner, Yeo Tiong Min, Alexander Di Stefano and Nicholas Liu, as well as to the Editor, Louise Gullifer, and the reviewers, for their comments which improved this article. Any errors are mine. Address for Correspondence: Yong Pung How School of Law, Singapore Management University, 55 Armenian Street, Singapore 179943. Email: [kwanhola@smu.edu.sg](mailto:kwanhola@smu.edu.sg).

<sup>1</sup> See e.g. G. McMeel, “Book Review: The Law of Assignment: The Creation and Transfer of Choses in Action” (2008) 37 C.L.W.R. 100, 101; A. Tettenborn, “Problems in Assignment Law: Not Yet Out of the Wood?” in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford 2010); C.H. Tham, “Book Review on the Law of Assignment” [2014] J.B.L. 520; P. MacMahon, “Rethinking Assignability” [2020] C.L.J. 288; Y.K. Liew, “Explaining Assignments of Arbitration Agreements” [2021] C.L.J. 101.

that “[n]ovation need not be left to ad hoc agreement; it is open to the parties to provide for it in advance and in particular to establish a contractual mechanism by which novation takes place automatically on the occurrence of a designated act or event.”<sup>2</sup>

Although put forward without supporting authority, this “advance consent” proposition unquestionably recorded a contemporary commercial practice. One example was the trading of loans, usually syndicated, on the UK secondary market beginning in the late 1980s. A loan agreement frequently contained a term allowing the lender at some future time to novate the agreement to a third-party bank or financial institution simply by delivering a prescribed document to a designated person (typically an agent bank). Thereafter the lender was released from its rights and obligations under the agreement, which would be novated to the incoming bank or institution. The borrower, unmoved through all of this, was not required to provide *ad hoc* consent to the novation, since the issue of consent was already covered by the antecedent term in the loan agreement.

What constitutes a novation is clear enough in English law, as is the general principle that parties must strictly perform the terms of their contracts. But put the two together as Goode suggests and one confronts a blurrier picture. The precise legal mechanism by which a subsequent novation is made effective pursuant to a prior agreement is theoretically intriguing. But that is not even the main difficulty, which lies in identifying the abuse to which the mechanism can be put and in devising the appropriate controls to be imposed. As we will see, the insalubrious aspects have not attracted judicial attention for the most part.<sup>3</sup>

This article examines the legal footing on which the operation of the advance consent proposition rests. It newly explores the risks in adopting a pristine version of the advance consent proposition in the law of novation and considers whether there are safeguards that should be embedded within the process of scrutiny, if in any case there arises concern over the

<sup>2</sup> R. Goode, *Commercial Law*, 2nd ed. (London 1995), 109. This was not in the first edition but has continued to feature in later editions: see R.M. Goode, *Commercial Law*, 3rd ed. (London 2004), 105; E. McKendrick (ed.), *Goode on Commercial Law*, 4th ed. (London 2012), 117; E. McKendrick (ed.), *Goode on Commercial Law*, 5th ed. (London 2016), [3.89]; E. McKendrick, *Goode and McKendrick on Commercial Law*, 6th ed. (London 2020), [3.92]. Goode had written earlier in 1988 that a novation “requires the assent of the borrower unless provided for in the loan agreement” and supplemented that statement in 2003 with a footnote that the “mechanism for novation can be agreed in advance”: see R.M. Goode, *Legal Problems of Credit and Security*, 2nd ed. (London 1988), 25; R. Goode, *Legal Problems of Credit and Security*, 3rd ed. (London 2003), [1–82], n. 87.

<sup>3</sup> It has been said that novation “in English domestic law lacks systematic development and exegesis”: M. Bridge, “The Proprietary Aspects of Assignment and Choice of Law” (2009) 125 L.Q.R. 671, 677, n. 38. The few academic studies that exist on common law novation are of high quality but do not delve into the risks of abuse: see e.g. E.A. Whitman, “Novation” (1891) 16 Am. Eng. Ency. Law 862; J.B. Ames, “Novation” (1892) 6 Harv. L. Rev. 184; H.W. Beall, “Novation” (1902) 21 Am. Eng. Ency. Law (2nd ed.) 659; W.L. Nixon Jr., “The Requisites and Effects of Novation: A Comparative Survey” (1950) 25 Tulane L. Rev. 100; M.P. Furmston, “The Assignment of Contractual Burdens” (1998) 13 J.C.L. 42; H.O. Hunter, “Commentary on ‘Assignment of Contractual Burdens’” (1998) 13 J.C.L. 51; J. Bailey, “Novation” (1999) 14 J.C.L. 189.

effectiveness of a novation that is undertaken pursuant to consent given in advance. These issues take on significance in light of the increasing frequency at which clauses are used in modern times, particularly in the commercial space, to cater for a party's prospective consent to a later novation. But first, before proceeding any further, we must consider the novation process and some developments that have attenuated its more formal elements over the years.

## II. CONSENT IN NOVATION

Many apprehend novation in a functional way and in contrast with assignment. Suppose *A* and *B* are the initial parties to a contract, and *C* is a stranger to them. English law generally allows *B* to assign its rights but not its obligations under the contract to *C*.<sup>4</sup> If *B* desires to "transfer" such rights and obligations it must obtain the consent, not just of *C*, but also of *A*, the unchanged party who takes the benefit of the performance of those obligations.<sup>5</sup>

This "transfer" is formally termed a substitutive novation and is itself a contract involving all of those persons.<sup>6</sup> In strict legal terms that results in the extinguishment of the original contract between *A* and *B* and the creation of a new contract between *A* and *C*. The overall effect is *B*'s transferring the whole contract (including the obligations) to *C*, who accepts such transfer and agrees to perform the contract (and the obligations); and *A*'s agreeing to this transfer and to look to *C* for the performance of those obligations, and its releasing *B* from such performance. The mutual acceptances and releases constitute the necessary consideration passing from each of them.<sup>7</sup>

A crucial element here is the requisite consent from each of *A* and *C*, encapsulated within their respective acceptances and agreement as described above. *C*'s consent to the novation is obviously vital as *B*'s obligations cannot generally be forcibly imposed on it. Intuitively, also, *A*'s consent to the novation is required; otherwise, *B* could unilaterally shift its obligations to *C*, who might be insolvent or simply someone with whom *A* did not want to contract. Upon deeper reflection, however, the inherent freedom to select one's contracting partners cannot be the sole reason for imposing a consent requirement. That has not stopped English law from recognising an assignment of a contractual *right* to performance without the obligor's consent; notice to the obligor suffices to bind it to the

<sup>4</sup> *Tollhurst v Associated Portland Cement Manufacturers (1900) Ltd.* [1902] 2 K.B. 660, 668 (Collins M. R.); *Linden Gardens Trust Ltd. v Lenesta Sludge Disposals Ltd.* [1994] 1 A.C. 85, 103 (Lord Browne-Wilkinson); *Kabab-Ji SAL v Kout Food Group* [2021] UKSC 48, [2021] Bus. L.R. 1717, at [60] (Lord Hamblen and Lord Leggatt).

<sup>5</sup> *Quest Advisors Ltd. v McFeely* [2009] EWHC 2651 (Ch), at [17] (Robin Knowles Q.C.).

<sup>6</sup> A novation may also be between *A* and *B* only, as where they agree to make a new contract and thereby expressly or impliedly discharge their original contract. Bipartite models of novation do not involve a stranger or raise attendant difficulties.

<sup>7</sup> It is common to see parties executing a novation in the form of a deed to forestall arguments of invalidity based on a lack of consideration.

assignee.<sup>8</sup> Instead, a somewhat consequentialist approach has been adopted on consent. Where a unilateral assignment of *rights* is permissible, it is said that the party who remains unchanged (i.e. the obligor) cannot object because it is all the same to the obligor who should receive its performance so long as its obligation is eventually discharged;<sup>9</sup> but in a hypothesised unilateral “transfer” of *obligations*, the unchanged party (i.e. the obligee) may validly object because it has a right to performance from the counterparty it selected, whom may have had unique characteristics that factored into its choice.<sup>10</sup>

Focussing on *A*'s consent, that must obviously be in substance to permit the novation of the contract (including the obligations therein) from *B* to *C*.<sup>11</sup> The *time* at which such consent may be provided is less clear. Although the latest moment is at the point of novation itself, it is conceivable – indeed it commonly happens – that there is a period of time between when consent is given and when the novation takes effect, such as where *A*, *B* and *C* execute an agreement providing, in terms, for the novation of an identified contract to become effective only at a later date upon satisfaction of a condition.<sup>12</sup> In this scenario the validity of *A*'s consent, contained in the novation agreement, should be above challenge. Provided that all the parties are identified in the agreement and the terms of the novation are certain and complete, the delay in effectiveness is but a mechanical aspect of the novation process and ought not to vitiate *A*'s consent, which remains

<sup>8</sup> This is the frontier of a debate (not covered here) about whether an assignment of rights is in fact based on a trust relationship rather than predicated on conceptions of transfer: see generally J. Edelman and S. Elliott, “Two Conceptions of Equitable Assignment” (2015) 131 L.Q.R. 228; C.H. Tham, *Understanding the Law of Assignment* (Cambridge 2019); A. Tettenborn, “Book Review: Understanding the Law of Assignment” [2020] L.M.C.L.Q. 693.

<sup>9</sup> Yet another established position (e.g. *Mulkerrins v PricewaterhouseCoopers* [2003] UKHL 41, [2003] 1 W.L.R. 1937, at [15] (Lord Millett)) which has occasionally been questioned: see latterly MacMahon, “Rethinking Assignability”, 310–11.

<sup>10</sup> *Kemp v Baerselman* [1906] 2 K.B. 604, 610 (Farwell L.J.); *Nokes v Doncaster Amalgamated Collieries Ltd.* [1940] A.C. 1014, 1019 (Viscount Simon L.C.); *Southway Group Ltd. v Wolff* (1991) 57 B.L.R. 33, 52 (Bingham L.J.). Exceptions to the rule that obligations may be shifted only with the consent of the obligee exist, one instance being the restrictive covenant attaching to real property and binding on any person who becomes the proprietor. There are other established (albeit limited) situations where, without the obligee's consent, the relevant obligation may be validly discharged by one who is not an original party to the contract, such as through delegated performance. Statutory provisions may also exceptionally allow for obligations to be shifted automatically upon occurrence of a specified event: see e.g. Co-operative and Community Benefit Societies Act 2014, s. 110 (predecessor provision discussed in *Stansell Ltd. v Co-operative Group (CWS) Ltd.* [2006] EWCA Civ 538, [2006] 1 W.L.R. 1704); Financial Services and Markets Act 2000, s. 112 (discussed in *WASA International (UK) Insurance Co. Ltd. v WASA International Insurance Co. Ltd.* [2002] EWHC 2698 (Ch), [2003] 1 B.C.L.C. 668, at [16]; *In re AIG Europe Ltd.* [2018] EWHC 2818 (Ch), [2019] Bus. L.R. 307, at [32]); Transfer of Undertakings (Protection of Employment) Regulations 2006, Regulation 4 (predecessor provision discussed in *British Fuels Ltd. v Baxendale* [1999] 2 A.C. 52, 76, [1998] 3 W.L.R. 1070). This article is not concerned with such exceptions, situations or provisions, save where they arise in an ancillary way to the discussion on novation.

<sup>11</sup> “The need for consent carries within it the need for a comprehension by the original parties as to what burden is being removed and to whom it is being transferred”: *Bambury v Jensen* [2015] NZHC 2384, at [42] (Fogarty J.).

<sup>12</sup> Accepted since at least *Ex parte South* (1818) 36 E.R. 907 and *Wilson v Coupland* (1821) 106 E.R. 1176.

proximately connected to the ultimate event of novation. Nor should the reasons for the interregnum be of legal moment. It would cause consternation if the courts were to insist on *A*'s consent being valid only if given at the effective time of novation.

Discussion of the obligee's consent is therefore framed by two primary inquiries: was consent given to the novation in question, and was that consent still valid at the effective time of novation? The outer limits of this requirement were soon explored. In addition to Goode, whose views have been mentioned, Justine Kirby theorised that an express term in the contract could enable *B* to subsequently "transfer" the contract (inclusive of rights and obligations) to *C* without needing *A*'s consent at the time of the transfer. She reasoned that *A* would, in a broader sense, have already provided its agreement to a transfer – albeit probably to transfers in general rather than a particular transfer – *at the time of the original contract* rather than at the time of transfer.<sup>13</sup> Kirby concluded: "[t]here is no compelling reason why a suitably worded prospective substitution provision should not enable a party to shed both its rights and obligations where these are assumed by another person."<sup>14</sup>

One last modern trend deserves mention. Given the state of English law in the late twentieth century, the only fail-safe way of "transferring" contractual obligations was to obtain the obligee's unqualified consent to a novation. The cumbrousness of the process eventually led commercial people to experiment with diluting the absolute nature of the consent requirement. For instance, after acknowledging that the obligee's consent had to be obtained for a novation, a contract term might state either that such consent was not to be unreasonably withheld,<sup>15</sup> that such consent was deemed to be given where the obligee failed to respond within a prescribed period after receiving notice of the obligor's intention to undertake a novation,<sup>16</sup> or that the obligee had irrevocably appointed the obligor to execute any requisite document on its behalf.<sup>17</sup> Yet another technique was to incorporate a term providing for the obligee's prospective consent to a later novation – the primary concern of this article.<sup>18</sup>

<sup>13</sup> J. Kirby, "Assignments and Transfers of Contractual Duties: Integrating Theory and Practice" (2000) 31 V.U.W.L.R. 317, 345.

<sup>14</sup> *Ibid.*, at 348.

<sup>15</sup> A.C. Gooch and L.B. Klein, *Documentation for Loans, Assignments and Participations* (London 1996), 307; J. Oldnall and M. Clark, "The Age of Consent" (2010) 25 J.I.B.L.R. 89; M. Bridge et al., *The Law of Personal Property*, 3rd ed. (London 2022), [25-006].

<sup>16</sup> R.P. Buckley, "The Law of Emerging Markets Loan Sales: Part 1" (1999) 14 J.I.B.L. 110, 111; A. Fight, *Syndicated Lending* (Oxford 2004), 117; M. Dunn et al., "The New Breed of Transfer Restrictions in Leveraged Lending Transactions: A New Paradigm or Just a Sign of the Times?" [2018] J.I.B.F.L. 222; contra Bailey, "Novation", 215.

<sup>17</sup> *Grant v WDW 3 Investments Ltd.* [2017] EWHC 2807 (Ch), at [12].

<sup>18</sup> There will almost certainly be further evolutionary stories which are outwith the scope of this article. For instance, on the use of blockchain technology in the transfer of syndicated loan interests, see e.g. S.J. Obie, "Blockchain and the Syndicated Loan Market: A Closer Look" [2017] J.I.B.F.L. 711; L. González-Echenique, "Blockchain: The Future of Syndicated Lending?" [2019] J.I.B.F.L. 326, 328.

### III. THE ADVANCE CONSENT PROPOSITION

Goode's description of the advance consent proposition (cited at the outset) may not be a comprehensive statement of the law, but it remains an accurate reflection of modern-day practice. Parties indeed purport by the terms of their contracts to agree in advance to the novation of the contract and in particular to establish a contractual mechanism by which novation takes place automatically on the occurrence of a designated act or event. This is usually done where the possibility of a subsequent novation is contemplated by the parties at the time of contracting.<sup>19</sup>

#### A. Scenarios

One of those possibilities relates to the secondary trading of assets, especially the disposal and acquisition of choses in action. In *Habibsons Bank Ltd. v Standard Chartered Bank (Hong Kong) Ltd.*<sup>20</sup> it was observed that a term effectively providing for "advance consent" to be given for a novation enabled lending institutions to freely transfer their interests in a syndicated loan to other banks and financial institutions that regularly engaged in investing in those assets. And in addition to generating profit and market liquidity, these types of transfers have a role in the distribution of capital and regulatory risks among participants in financial systems.<sup>21</sup>

The usage of such terms also allows for the more efficient entry and exit of parties who are in long-term contractual relationships.<sup>22</sup> The archetype is the relationship among partners or shareholders. Partnerships and companies often experience changes in their constitution, such as where existing persons leave and new persons join as partners or shareholders. To avoid recurrent execution of paperwork and formalities, each partner or shareholder gives its prior assent in the relevant partnership or shareholder agreement to the future accession thereto of any person who fulfils the stipulated conditions of entry.<sup>23</sup>

Yet a further motivation for inserting an "advance consent" term is to attain greater flexibility in relation to future allocations of interests within a larger corporate or organisational structure.<sup>24</sup> A contracting party (such as *B*, the obligor in our scenario) might desire at a later time to effectively transfer its interest in the contract to a person related to it, usually but not always in the course of a future restructuring or consolidation exercise. Consent from the other party (*A*, the obligee) could be viewed as redundant

<sup>19</sup> Bailey, "Novation", 217–18.

<sup>20</sup> [2010] EWCA Civ 1335, [2011] Q.B. 943, at [21] (Moore-Bick L.J.).

<sup>21</sup> R. Goode, *Commercial Law in the Next Millennium* (London 1998), 11; Dunn et al., "New Breed of Transfer Restrictions", 223.

<sup>22</sup> See e.g. *216 Jamaica Avenue LLC v S & R Playhouse Realty Co.* 540 F. 3d. 433 (6th Cir. 2008), 438–39.

<sup>23</sup> See e.g. *Byrne v Reid* [1902] 2 Ch. 735; *Kynixa Ltd. v Hynes* [2008] EWHC 1495 (QB).

<sup>24</sup> Kirby, "Assignments and Transfers of Contractual Duties", 348.

in that case. If, therefore, such a future transfer – called a related party transfer – were already contemplated at the time of execution of the contract, the mechanism therefor could be stipulated in the contract itself.<sup>25</sup>

### B. Unilateral Contract Theory

There is consequently some commercial justification for the insertion of a contract term by which one party, *A*, consents in advance to the other, *B*, being able to subsequently novate the contract to a stranger, *C*. But that does not disclose the precise legal footing on which the operation of such a term or the advance consent proposition rests.

In English law that is commonly explained by enlisting the use of unilateral contract theory. An appropriately worded term in the original contract, while setting out the novation mechanism, is viewed as implicitly containing two standing offers as well. The first offer, to discharge that contract upon such conditions as might be set out in the novation mechanism, is made by *A* to *B*. The second offer, to conclude a new contract on the terms provided in the novation mechanism, is made by *A* to all eligible persons in the stated class.<sup>26</sup> *B* and *C* (the putative incoming party) are not obliged to, but may, respectively accept these offers by satisfying and taking the relevant conditions and actions prescribed in the novation mechanism. Acceptance by *B* of the offer directed to it converts the unilateral contract between *A* and *B* into a new synallagmatic contract between them in which they agree to discharge the original contract; while acceptance by *C* of the offer directed to it converts the unilateral contract between *A* and *C* into a new synallagmatic contract between them on the terms provided in the novation mechanism.<sup>27</sup> Together these synallagmatic contracts constitute the effective novation of the original contract from *B* to *C*, and, importantly, no overt action by *A* is necessary at the time of novation.

Banking law practitioners had postulated a unilateral contract analysis as early as in 1987.<sup>28</sup> As mentioned, the proposition that an obligee could

<sup>25</sup> See e.g. *CSG Ltd. v Fuji Xerox Australia Pty. Ltd.* [2011] NSWCA 335.

<sup>26</sup> Since at least *Carlill v Carbolic Smoke Ball Co.* [1892] 2 Q.B. 484 (affid. [1893] 1 Q.B. 256) English law has accepted the validity of a contract formed on the basis of an offer made to the world at large.

<sup>27</sup> “Synallagmatic” having here its English contract law meaning: see *United Dominions Trust (Commercial) Ltd. v Eagle Aircraft Services Ltd.* [1968] 1 W.L.R. 74, 82–84 (Diplock L.J.); *Harvela Investments Ltd. v Royal Trust Co. of Canada (C.I.) Ltd.* [1986] A.C. 207, 224–26 (Lord Diplock).

<sup>28</sup> M. Hughes, “Transferability of Loans and Loan Participations” [1987] J.I.B.F.L. 5, 7–8; J.M. Walter and S.A. Rechenberg, “The Role of Banks as Principal Bridging Financiers” (1991) 65 Aust. L.J. 703, 715; F. Graaf, *Euromarket Finance: Issues of Euromarket Securities and Syndicated Eurocurrency Loans* (Deventer 1991), 378; T. Rhodes (ed.), *Syndicated Lending: Practice and Documentation* (London 1993), 303; A. Fight and G. Le F. Shepherd, *Syndicated Lending: The Legal Framework* (London 1996), 27–28; M. Hughes, “Contracts, Consideration and Third Parties” [2000] J.I.B.F.L. 79, 81; M. Hughes, “Loans Agreements – Single Bank and Syndicated” [2000] J.I.B.F.L. 115, 118–19. The unilateral contract analysis may not have been uniformly received within the industry; in T.M. Lennox, “Transfer of Obligations” (2001) 2 Melb. J. Int. L. 209, 210–12, reference was made to the difficulties in rationalising the substitution of lenders in syndicated loan arrangements without mentioning the unilateral contract analysis.



effectively give its consent to a novation in advance held attraction for secondary debt market participants because it enabled banks and financial institutions to sell and purchase loan interests without the borrower's active involvement. Unsurprisingly, judicial endorsement of this repurposed use of unilateral contracts arrived in a pair of cases dealing with loan interests acquired on the secondary market.

In *Argo Fund Ltd. v Essar Steel Ltd.*<sup>29</sup> a borrower had entered into a loan facility agreement with a syndicate of banks for an aggregate principal amount of US\$40 million. The facility was fully drawn down. Some years later, an investment company purchased various tranches of that debt amounting to a nominal value of US\$29.5 million on the secondary market. The borrower's subsequent failure to repay the debt resulted in a claim for breach of contract brought by the investment company, which argued that it had purchased the relevant loan interests in accordance with the terms of the original facility agreement. These were the relevant terms:

27.1 This Agreement shall be binding upon and inure to the benefit of each party hereto and their respective successors, Transferees and assigns . . . Any Bank may, subject to the execution and completion of such documents as the Agent may specify and with notice to the Borrower assign all or any of its rights and benefits hereunder or, subject to the payment to the Agent of a transfer fee of US\$250, transfer in accordance with clause 27.2 all or any of its rights, benefits and obligations hereunder.

27.2 If any Bank wishes to transfer all or any of its rights, benefits and/or obligations hereunder, then such transfer may be effected by the delivery to the Agent of a duly completed and duly executed Transfer Certificate in which event, on the later of the effective date of transfer (the "Transfer Date") specified in such Transfer Certificate and the third business day after the date of delivery of such Transfer Certificate to the Agent:

- (i) to the extent that in such Transfer Certificate the Bank party thereto seeks to transfer its rights and obligations hereunder, the Borrower and such Bank shall be released from further obligations towards one another hereunder and their respective rights against one another shall be cancelled (such rights and obligations being referred to in this clause 27.2 as "discharged rights and obligations");
- (ii) the Borrower and Transferee party thereto shall assume obligations towards one another and/or acquire rights against one another which differ from the discharged rights and obligations only insofar as the Borrower and the Transferee have assumed and/or acquired the same in place of the Borrower and such Bank; and
- (iii) . . . the Transferee and the other Banks shall acquire the same rights and assume the same obligations between themselves as they would have acquired and assumed had the Transferee been an original party hereto

<sup>29</sup> [2005] EWHC 600 (Comm), [2005] 2 Lloyd's Rep. 203.

as a Bank with the rights and/or obligations acquired or assumed by it as a result of such transfer.<sup>30</sup>

Aikens J. in the Commercial Court accepted that clauses 27.2(i) and 27.2(ii) had the effect of novating the agreement between the borrower and the original syndicated participant to the borrower and the investment company.<sup>31</sup> He noted that clause 27.2 in terms permitted the original participant to transfer its rights and obligations simply by delivering a completed Transfer Certificate to the agent bank.<sup>32</sup> Addressing, then, the borrower's lack of active involvement at the time of such transfer, Aikens J. agreed with the unilateral contract analysis and construed the mechanism in clause 27.2 as incorporating two standing offers by the borrower that could respectively be accepted by the original participant and the investment company.<sup>33</sup> Reading Aikens J.'s decision, it is clear that not only was he navigating uncharted waters at the time,<sup>34</sup> he understood his ruling to uphold the effectiveness of clause 27.2 to give imprimatur to the dispensation of the borrower's consent at the time of novation, with the borrower's being required only to have assented to the transfer clause contained in the original facility agreement.

The second case is *Habibsons Bank*, also involving a syndicated loan arrangement. The borrower had entered into a facility agreement for US \$117.5 million to be lent by a syndicate of banks. One of the syndicate banks subsequently agreed to sell US\$2 million of its share of the loan to another bank. At around that time, however, the borrower became insolvent and unable to meet its obligations under the facility agreement. This was the catalyst for a dispute between the selling and purchasing banks over the transfer of the US\$2 million loan share. The selling bank debited the settlement amount from funds held with it by the purchasing bank, which then brought proceedings to recover that amount. It was argued that because the purported transfer of the loan by the selling bank involved a partial novation of the facility agreement, it was necessary to obtain the borrower's consent to the transaction, and that was never given.

<sup>30</sup> Terms apparently based on a standard form issued in 1997 by the Loan Market Association: S. Howe, "Defining a Financial Institution" (2006) 156 N.L.J. 1280. See M. Hughes, "Creating a Secondary Market in Loans: A Review of the Key Issues" [1998] J.I.B.F.L. 352 for an overview of the standard documentation for syndicated loans around 1997 and 1998.

<sup>31</sup> *Argo Fund Ltd. v Essar Steel Ltd.* [2005] EWHC 600 (Comm), [2005] 2 Lloyd's Rep. 203, at [50].

<sup>32</sup> As Aikens J. pithily put it (at [50]), "nothing more has to be done".

<sup>33</sup> *Ibid.*, at [51]–[52]. On appeal, the leading judgment delivered by Auld L.J. did not discuss the unilateral contract analysis, although it was accepted that clause 27.2 did contain a mechanism for novation: *Argo Fund Ltd. v Essar Steel Ltd.* [2006] EWCA Civ 241, [2006] 2 Lloyd's Rep. 134, at [18], [63].

<sup>34</sup> No relevant authority appeared to have been cited to Aikens J. for this repurposing of the unilateral contract. Indeed, according to one commentator who has a claim to being the inventor of the original "transferability" provisions in syndicated lending agreements, *Argo Fund* was the first ever judicial endorsement of the unilateral contract analysis in a syndicated lending context: M. Hughes, *Legal Principles in Banking and Structured Finance*, 2nd ed. (Haywards Heath 2006), 123; M. Hughes, "Transferability in Syndicated Lending" (2007) 1 L.F.M.R. 21, 23.

Similar to *Argo Fund*, the facility agreement in *Habibsons Bank* contained detailed provisions for the transfer of a lender's rights and obligations. In the Commercial Court, Cooke J. found them to prescribe a clear mechanism for the novation process. He fully recognised what was taking place – a party (here, the borrower) was consenting in advance to a means of novation that would subsequently be binding upon it at the election of another party – and gave three justifications in support of its effectiveness. The parties had expressly agreed on what was to happen and the means by which the novation was to become operative; the bundle of rights and obligations transferred remained the same, so that the borrower could have had no realistic concern as to the identity of any new lender in circumstances where the lenders had already fulfilled their part of the bargain in providing the loan; and it was commonplace for novations to occur on the basis of such clauses in syndicated loan agreements, many of which would have to be re-drafted if found ineffective.<sup>35</sup>

On appeal, the requirement for an obligee to have to consent to a novation was reaffirmed by the Court of Appeal. But, in a judgment with which Rix L.J. agreed, Moore-Bick L.J. reasoned that such consent could be contained in the initial agreement itself, so that any subsequent novation might be done in the manner prescribed in the agreement without the obligee's further consent – or what he termed a specific consent – to the novation. Consideration for that advance consent was given by the obligor's entry into the initial agreement. As to how the novation could have taken place later without the obligee's specific consent, Moore-Bick L.J. indicated that he found persuasive the unilateral contract analysis suggested in *Argo Fund*.<sup>36</sup>

The reasoning deployed in *Habibsons Bank* clarifies several matters. It establishes at Court of Appeal level that, in a syndicated loan context, a party to the facility agreement may by a term thereof provide its consent to a subsequent novation of that agreement (and of the bundle of rights and obligations contained therein) by its counterparty to a stranger. The effectiveness of any such novation can be rationalised on the unilateral contract analysis. The agreement must also harbour a mechanism for the novation which is not nebulous, and there must be sufficient certainty as to the terms of the new contract subsequently formed between the obligee and the incoming party after the novation.<sup>37</sup> In *Habibsons Bank*, the relevant clauses mentioned the transfer of the outgoing lender's rights and

<sup>35</sup> *Habibsons Bank Ltd. v Standard Chartered Bank (Hong Kong) Ltd.* [2010] EWHC 702 (Comm), at [28].

<sup>36</sup> *Habibsons Bank Ltd. v Standard Chartered Bank (Hong Kong) Ltd.* [2010] EWCA Civ 1335, [2011] Q.B. 943, at [19], [21]–[23]. The Dutch law aspect of the case is noted in A. McKnight, "A Review of 2010: Part 1" (2011) 5 L.F.M.R. 3, 10.

<sup>37</sup> *Ibid.*, at [21]–[22].

obligations by means of a novation;<sup>38</sup> the dispensation of the borrower's specific consent for such a transfer; and the agent bank's active involvement in executing a Transfer Certificate delivered to it by the outgoing and incoming lenders. In this way there was a reasonably clear acknowledgment of the nature of the transfer and the dispensation of the borrower's specific consent, lending greater certainty overall to the operation of the novation mechanism.<sup>39</sup>

#### IV. OF RISK AND REWARD

*Argo Fund* and *Habibsons Bank* have not generated much adverse commentary on the correctness or utility of the advance consent proposition or the unilateral contract analysis.<sup>40</sup> In the loans context they have been uncritically mentioned or followed by later courts,<sup>41</sup> and the unilateral contract analysis has been proffered in explanation of a one-sided accession to a shareholder agreement.<sup>42</sup> The applicability of the advance consent proposition is no longer even constrained to lending or shareholder

<sup>38</sup> See also *Bailey v Barclays Bank plc* [2014] EWHC 2882 (QB), at [76] (H.H.J. Keyser Q.C.).

<sup>39</sup> Compared to the provision in *Argo Fund*, the wording in *Habibsons Bank* appears more elaborate and to have been based on an industry precedent issued by the Loan Market Association in 2004. It is unclear if the drafters of the loan agreement had the benefit of considering the judgments in *Argo Fund*.

<sup>40</sup> Academic writers and industry commentators generally have not been critical in their scrutiny. From the former, see A. Mugasha, *The Law of Multi-bank Financing: Syndicated Loans and the Secondary Loan Market* (Oxford 2007), [8.07]; E.P. Ellinger, E. Lomnicka and C.V.M. Hare, *Ellinger's Modern Banking Law*, 5th ed. (Oxford 2011), 788; A.G. Guest, *Guest on the Law of Assignment* (London 2012), [1-65] (see also the later editions A.G. Guest and Y.K. Liew, *Guest on the Law of Assignment*, 2nd ed. (London 2015), [1-72]; Y.K. Liew, *Guest on the Law of Assignment*, 3rd ed. (London 2018), [1-57-1-58]; Y.K. Liew, *Guest on the Law of Assignment*, 4th ed. (London 2021), [1-74-1-75]); M. Furmston and G.J. Tolhurst, *Privity of Contract* (Oxford 2015), [3.57], n. 228; G. Tolhurst, *The Assignment of Contractual Rights*, 2nd ed. (Oxford 2016), [3.06], n. 20; R. Cranston et al., *Principles of Banking Law*, 3rd ed. (Oxford 2017), 485; R. Goode and L. Gullifer, *Goode and Gullifer on Legal Problems of Credit and Security*, 6th ed. (London 2017), [1-87], n. 452; S. Paterson and R. Zakrzewski (eds.), *McKnight, Paterson, and Zakrzewski on the Law of International Finance*, 2nd ed. (Oxford 2017), [12.7.3.1-12.7.3.3]; J. Odgers (gen. ed.), *Paget's Law of Banking*, 15th ed. (London 2018), [12.30]; M. Smith and N. Leslie, *The Law of Assignment*, 3rd ed. (Oxford 2018), [5.113]; Tham, *Understanding the Law of Assignment*, 56; R. Zakrzewski and G. Fuller, *McKnight and Zakrzewski on the Law of Loan Agreements and Syndicated Lending* (Oxford 2019), [4.68-4.71]; L. Gullifer and J. Payne, *Corporate Finance Law: Principles and Policy*, 3rd ed. (Oxford 2020), 459; M. Bridge (gen. ed.), *Benjamin's Sale of Goods*, 11th ed. (London 2021), [23-318]; Bridge et al., *Law of Personal Property*, [25-004-25-005]. From the latter, see A. McKnight, "A Review of Developments in English Law During 2005" (2006) 21 J.I.B.L.R. 117, 133-34; G. Bhattacharyya and H. Beal, "The Meaning of 'Financial Institution': *Argo Fund Ltd. v Essar Steel Ltd.*" (2006) 21 J.I.B.L.R. 599, 600; Hughes, "Transferability in Syndicated Lending", 22-23; F. Julien, "Syndicated Financing and Transfer of Rights and Obligations: French and English Law Aspects" (2008) 2 L.F.M.R. 132, 137; M. Lovell and B. Vuong, "Goodridge Appeal: Legal Principles Governing Assignment and Novation of Contracts" (2011) 26(8) Australian Banking & Finance Law Bulletin 118; P. Rawlings, "Restrictions on the Transfer of Rights in Loan Contracts" [2013] J.I.B.F.L. 543; N. Mugarura, "The Law Relating to Syndicated Loan Agreements and Its Application in Commercial Practice" (2016) 24 J.F.R. & C. 177, 192.

<sup>41</sup> *Deutsche Bank A.G. v Unitech Global Ltd.* [2013] EWHC 471 (Comm), at [50] (Cooke J.); *Standard Chartered Bank (Hong Kong) Ltd. v Independent Power Tanzania Ltd.* [2016] EWHC 2908 (Comm), at [46] (Flaux J.). In Australia, see *Leveraged Equities Ltd. v Goodridge* [2011] FCAFC 3, (2011) 274 A.L.R. 655, at [299]-[328] (Jacobson J.); *GE Commercial Corporation (Australia) Pty. Ltd. v Wallis* [2015] NSWSC 704, at [21] (Adams J.).

<sup>42</sup> *Yara Australia Pty. Ltd. v Oswal (No. 2)* [2013] WASCA 187, at [67] (McLure P.), [424] (Murphy J.A.).

agreements, but potentially extends to other contracting contexts in general,<sup>43</sup> subject to the operation of contrary legislation.<sup>44</sup> The implications, however, are not all positive. Luxmoore J.'s early and tantalising suggestion in *De Tchihatchef v Salerni Coupling Ltd.*<sup>45</sup> that a cleverly worded substitutive provision might allow the substituted party to liberate itself from liability points to a recurrent inquiry in this area: the law's striking of a proper balance between contractual autonomy and the concern that obligors might unfairly shed their burdens. This section discusses three overlapping difficulties and some potential methods of resolution.

### A. Abuse

The first and most apparent difficulty is encapsulated within the following statement of HHJ Peter Bowsher Q.C. in *St. Martin's Property Corporation Ltd. v Sir Robert McAlpine & Sons Ltd.*: "English law has long set its face against the assignment of liabilities or burdens, for otherwise a party to a contract might avoid his responsibility by assigning, for example, the duty to make payment to a man of straw or a worthless £100 company."<sup>46</sup>

In the past two decades the courts do not appear to have fully heeded this brand of caution when developing a theory of advance consent to novation,<sup>47</sup> instead largely being content to frame the proposition in unqualified terms.<sup>48</sup>

One explanation for this is that almost all of the existing authorities have centred over commercial parties rather than private individuals. There is no instinctive offensiveness about the notion that such a party should look after itself and swallow the consequences if in fact it has consented in advance to the counterparty's unilaterally novating the contract (and its contained obligations) to an unknown stranger. This underlies Kirby's recognition – and dismissal – of the risk as something the obligee may guard against by introducing restrictions on the type of person as a potential novatee.<sup>49</sup>

<sup>43</sup> Such as a conditional fee agreement (*Budana v Leeds Teaching Hospitals NHS Trust* [2017] EWCA Civ 1980, [2018] 1 W.L.R. 1965), petroleum exploration agreement (*Armour Energy Ltd. v AEGP Australia Pty. Ltd.* [2016] QSC 153, at [61]–[65]) or construction and design contract (*Energy Works (Hull) Ltd. v MW High Tech Projects UK Ltd.* [2020] EWHC 2537 (TCC), [2020] B.L.R. 747, at [102]).

<sup>44</sup> A possible instance being the Consumer Rights Act 2015, s. 63, read with Schedule 2, paragraph 7. [1932] 1 Ch. 330, 345–46.

<sup>45</sup> [1932] 1 Ch. 330, 345–46.

<sup>46</sup> (1991) 25 Con. L.R. 51, 60.

<sup>47</sup> Cf. the academic views in R.P. Buckley, "Domestic and Euromarket Loan Transfers Under the Corporations Law" (1993) 67 Aust. L.J. 828, 830; Kirby, "Assignments and Transfers of Contractual Duties", 348; K.H. Lau, "Unilateral Transfers of Contractual Obligations" (2013) 129 L.Q.R. 491, 494; T.N. Parsons, *Lingard's Bank Security Documents*, 7th ed. (London 2019), [12.30] (with a reference to J.R. Lingard, *Tolley's Commercial Loan Agreements* (Croydon 1990), [19.2]).

<sup>48</sup> A similar observation may be made of the state of Australian law, which contains little examination of the possible limits to the advance consent proposition: see e.g. *Pacific Brands Sport & Leisure Pty. Ltd. v Underworks Pty. Ltd.* [2006] FCAFC 40, (2006) 230 A.L.R. 56, at [32] (Finn and Sundberg JJ.); *Leveraged Equities v Goodridge* [2011] FCAFC 3, at [299]–[317] (Jacobson J.).

<sup>49</sup> Kirby, "Assignments and Transfers of Contractual Duties", 348.

The reality is that, as seen earlier, commercial parties are often motivated to incorporate an “advance consent” term into their legal contracts, including contracts entered into with private individuals and others who do not stand in a position of similar strength. In recent years the increase in the number of cases examining “advance consent” terms and the different types of contracts they consider indicates that parties with greater bargaining power are catching on and successfully introducing “advance consent” clauses into their legal agreements. It is not clear then that restrictions of the sort envisaged by Kirby are easily inserted at all by obligees. The upshot is the requirement for an obligee to consent to a novation fast becoming an increasing formality.

Another reason for the dearth of judicial concern over unfair disposals of liabilities by obligors is that those scenarios do not seem to reach the courts for decision. In *Habibsons Bank*, where the most sustained discussion of the advance consent proposition in modern English law can be found, no unsavoury practices or unsophisticated parties were present that necessitated mention by the Court of Appeal of possible exceptions to the proposition. Indeed, apart from a rare question from time to time, the English courts have phrased the advance consent proposition in quite general terms. We will later have to make the most out of those qualifications.

### *B. Unperformed Obligations*

The second difficulty is inherent in a situation where the contractual obligations of the obligor, *B*, are not fully performed (that is, where the contract is executory) at the point of novation by *B* to the novatee, *C*. This may not be the result of a deliberate attempt by *B* to avoid liability for non-performance, which distinguishes it from the abuse scenario described earlier.

Take the following hypothetical modelled after the facts of *Argo Fund* and *Habibsons Bank*. A borrower has entered into a facility agreement for £10 million to be lent in equal shares by Banks *X* and *Y*. Bank *X* then sells its £5 million share of the loan to Bank *Z* on the secondary market, and they consequently follow the novation procedure prescribed in the facility agreement in the same way the selling and purchasing banks did in *Argo Fund* (recall that this eliminates the borrower’s active participation in the novation). No part of the loan has been disbursed yet to the borrower under the facility at the time of sale and undertaking of the novation procedure. Two weeks after that procedure is completed, the borrower writes to Bank *Z* requesting for a draw-down of £5 million on the loan facility – they being respectively the obligee and obligor – and is surprised to find its request rebuffed on the ground that an application had been filed the previous week by a major creditor of Bank *Z* to place the bank in liquidation.

Leaving aside the application of insolvency rules, the borrower's immediate recourse would be to consider pursuing an action in breach of contract against Bank Z. With the commencement of the latter's liquidation proceedings, however, that option is likely to be cold comfort for the borrower, particularly so if it had required the funds urgently for business purposes. It may be left rueing its decision to consent in advance to a future novation of the agreement by Bank X to an unknown entity. To be sure, this outcome is not unique to an advance consent scenario – it could have occurred even if the borrower had participated actively in the novation process, such as where the borrower, Bank X, Bank Y and Bank Z had all executed a standalone novation agreement – but the likelihood of its arising is greater where the borrower has consented to the novation in advance, owing to the lack of opportunity for scrutinising the novatee around the time of novation.

Allowing the borrower to sue Bank X for the funds, on the other hand, runs up against the seemingly irrepressible objection that the purported novation has already discharged the contract between them. The logic that either Bank X or Bank Z, *but not both at the same time*,<sup>50</sup> can be liable for the obligation to advance funds to the borrower is rendered the more compelling where wording exists to that effect in the novation provisions within the facility agreement.<sup>51</sup>

All of this leads, in the absence of statutory intervention, to a curious problem for the borrower (or any obligee in an analogous scenario). The ordinary understanding of the common law effects of a multipartite novation – even one operating on the basis of the obligee's advance consent – which is often reinforced by the detailed provisions found in the underlying agreement suggests that the obligee must, after the novation, look exclusively to the novatee for performance of the obligations originally borne by the obligor. There is of course little difficulty where there are no obligations left under the contract for the novatee to perform. But if such obligations do exist then the neat theoretical dichotomy just described potentially unravels in practice, since the obligee's non-participation at the point of novation ordinarily results in an inability to scrutinise or veto the novatee, who may be incapable or less capable than the outgoing obligor with respect to the performance of the relevant obligations. Any eventual deficiency in performance by the novatee leaves the obligee between two stools.

<sup>50</sup> See further Bailey, "Novation", 201.

<sup>51</sup> By the same token, though, claiming that the original contract has been discharged pursuant to such wording may (inadvertently) trigger a statutory prohibition against that action: see e.g. Consumer Rights Act 2015, s. 63 (read with Schedule 2, paragraph 7) which may render unfair and therefore non-binding on a consumer a one-sided term having the object or effect of authorising a trader to dissolve the contract on a discretionary basis. No court or tribunal appears to have ruled on this yet.



We may rule out the less attractive ways of addressing this. Ignorance, for one, is unlikely to be helpful. The aforesaid disjoint between theory and practice cannot be evaded on the ground that it will rarely arise in everyday contracting. A revolving credit facility in a syndicated lending agreement, for instance, which is in common usage, functions effectively *because* a lender – who might be substituted later – is continuously obligated to lend to the borrower from time to time during the term of the facility, provided the latter keeps within the facility limit and makes repayment as stipulated. Commercial realities therefore mean that the problem cannot be wished away. A solution more often advanced is that it is for an obligee to acquire its own protection by imposing conditions on the type of person who can be a novatee under the “advance consent” provision, such as in *Habibsons Bank* where it was stated that any prospective novatee had to be a “bank or financial institution . . . regularly engaged in or established for the purpose of making, purchasing or investing in loans, securities or other financial assets”;<sup>52</sup> and, where each of the conditions is satisfied, the obligee cannot then complain if the novatee is revealed to be incapable of performing the obligations. As adverted to earlier, however, the efficacy of this solution rests on the assumption that obligees can negotiate for such conditions to be installed. A large corporate borrower may successfully do so, but since the “advance consent” term can be used in numerous scenarios, many more who come up against one will not possess the ability as against their commercial counterparties to insert protective conditions.

It will be recalled that, at first instance in *Habibsons Bank*, Cooke J. upheld the effectiveness of an “advance consent” term partially on the ground that the borrower could have had no realistic concern as to the identity of the new (incoming) lender in circumstances where the lenders had already fulfilled their part of the bargain in providing the loan to the borrower.<sup>53</sup> This seems to suggest that if the lending obligation had *not* been fulfilled yet by the outgoing lender at the point of novation, questions might have been raised over the efficacy of the “advance consent” term. Whether (and if so how) that sort of instinctive recoil can be justified and explained is canvassed in a later section. We must round off the present discussion by considering a third difficulty relating to an “advance consent” provision.

### C. Partial Novation

The last difficulty engendered by the use of an “advance consent” term which is discussed here involves the so-called “partial novation” phenomenon. Although it may occur in any multipartite novation, the likelihood of

<sup>52</sup> See also *Galer v Mond* [2021] EWHC 1952 (Ch), at [29] (H.H.J. Stephen Davies).

<sup>53</sup> *Habibsons Bank v Standard Chartered Bank* [2010] EWHC 702 (Comm), at [28].



that is (again) greater in a situation where an “advance consent” term is relied on to effect the novation. Such a term is frequently adopted in a multipartite contracting context, where it is perceived to have the advantage of rendering subsequent novations more efficient by eliminating the active participation of the unchanged parties to the underlying contract.

Partial novation as a concept requires some unpacking. The nomenclature gained prominence following the Court of Appeal’s decision in the conjoined appeals of *Graiseley Properties Ltd. v Barclays Bank plc* and *Deutsche Bank AG v Unitech Global Ltd.*<sup>54</sup> which was delivered after the public discovered the manipulation of the London Inter-Bank Offered Rate (LIBOR) by a number of banks. The *Deutsche Bank* proceedings concerned a credit facility agreement pursuant to which US\$150 million had been lent to Unitech Global, with interest on the sum determined by reference to LIBOR. Deutsche Bank was the original lender but eight other lenders subsequently acceded to the credit facility agreement (the form of accession is elaborated on shortly). These nine lenders later sued Unitech Global for defaulting on the repayment of the loan, only to be met with a counter-allegation that Deutsche Bank had made certain representations to Unitech Global, primarily relating to the integrity of the bank’s role in the LIBOR-setting process, which had not only induced Unitech Global to enter into the credit facility agreement but were, given the bank’s actions in the rate-fixing scandal, false.

An application by Unitech Global to amend its pleadings to incorporate those misrepresentations failed before Cooke J. for reasons we need not cover in detail. It was specifically held in relation to the issue of remedies, though, that to the extent Unitech Global had any right to rescind the credit facility agreement as a result of Deutsche Bank’s misrepresentations, that right was lost when two of the eight lenders who acceded to the agreement did so by means of express novation which extinguished the original credit facility agreement and replaced it with new agreements. In the judge’s words, the effect of novation was “not simply to assign or transfer a right or liability, but to extinguish the existing agreement and create a new contract”.<sup>55</sup> Cooke J. was persuaded in part by the language used in the “advance consent” term, which mentioned transfers “by way of novation” and, it may be added, bore some resemblance to the one he had previously encountered in *Habibsons Bank*.

Unitech Global appealed against Cooke J.’s decision. On the novation issue, Longmore L.J. (with whom Underhill L.J. and Sir Bernard Rix agreed) did not dispute that a novation in the strict legal sense – involving the discharge of an existing contract and the creation of a new contract – had the effect of defeating any equities (such as the right to rescind)

<sup>54</sup> [2013] EWCA Civ 1372.

<sup>55</sup> *Deutsche Bank v Unitech Global* [2013] EWHC 471 (Comm), at [50].

which might apply to the existing contract.<sup>56</sup> Where he differed from the lower court was on the issue of whether such a novation was contemplated by the parties and had actually occurred in the present case. While the “advance consent” term mentioned transfers by way of novation, it also stated that a new incoming lender became “a Lender under this Agreement and . . . bound by the terms of this Agreement as a Lender”. Since parties would not, in a true novation, be agreeing to be bound by the existing agreement at all, Longmore L.J. wondered whether the term “novation” was being used in its strict legal sense in the “advance consent” provision.<sup>57</sup> And because it was arguable that the answer was in the negative – resulting in any right to rescind for misrepresentation remaining extant – the permission to amend application should not have failed on this ground.

The other point of immediate relevance is found within Longmore L.J.’s remarks about the fact that, even if two of the eight new lenders had acceded to the agreement by way of novation in the strict legal sense, the other six had acceded “by way of assignment, assumption and release of [the existing lender’s] rights or obligations”. According to him:

there must at least be an argument that, on the facts of the present case, there is only a partial novation so that [two lenders] became parties to a new contract freed of the equity of rescission whereas the other parties (whether the original or the other new lenders) remain bound under “this Agreement” and will be affected by any such equity.<sup>58</sup>

Adding that the concept of partial novation was not free from difficulty, Longmore L.J. nevertheless said that the problems ought not to be addressed on an application for permission to amend.<sup>59</sup> Although he did not do so he could have cited here the summary judgment decision of *Langston Group Corp v Cardiff City Football Club Ltd.*<sup>60</sup> where Briggs J. had said that the substitution of a stranger for an existing obligor in relation to some, but not all, of the obligations, leaving the remaining obligations unaffected as between the obligee and the obligor, did not seem obviously a case of novation of the entire contract.<sup>61</sup>

<sup>56</sup> *Graiseley Properties Ltd. v Barclays Bank plc* [2013] EWCA Civ 1372, at [33], [37].

<sup>57</sup> *Ibid.*, at [35]. In *Energy Works v MW High Tech Projects* [2020] EWHC 2537 (TCC), O’Farrell J. accepted (at [98]) that the label given by the parties was not conclusive and that each contract had to be construed against the relevant factual matrix.

<sup>58</sup> *Ibid.*, at [37].

<sup>59</sup> These problems did not in the event require to be resolved at trial: *Deutsche Bank A.G. v Unitech Global Ltd.* [2019] EWHC 969 (Comm), at [49] (Knowles J.).

<sup>60</sup> [2008] EWHC 535 (Ch), at [42].

<sup>61</sup> Briggs J. concluded that “the question whether the addition of a new party to an agreement, and its substitution as obligor for an existing party in respect of some, but not all of that party’s obligations under the contract gives rise to a determination of the old contract and its replacement with a new one is not susceptible of a single doctrinaire answer, applicable for all purposes. It will always be relevant to know for what purpose the question needs to be answered”: *ibid.*, at [47]. This scenario has been described as representing an “uncommon type of novation”: Bailey, “Novation”, 193. In Canada, see *Weldwood-Westply Ltd. v Cundy* [1965] S.C.R. 586, 591 (Spence J.)

This sketch of the “partial novation” concept presents several puzzles. There are initial questions over authoritativeness: given the nature of the application before the Court of Appeal, its views may be of limited precedential value and more liberally departed from in future cases.<sup>62</sup> The concept also opens a doctrinal Pandora’s Box. It seems to have been implicitly assumed in *Deutsche Bank* that contractual rights *and* obligations (at least in a loan context) might arguably be transferrable from a contracting party to a stranger by means of express *assignment and assumption*, subject to the latter’s being bound by any equities affecting the former at the point of transfer – the gist of the Court of Appeal’s reasoning – and with the transferee becoming solely responsible for the performance of the obligations.<sup>63</sup> Even accounting for the early stage of the proceedings, it is improbable that so distinguished a constitution of the court would have omitted to recognise that undergirding premise. This aspect of the decision is therefore more compellingly understood as representing the court’s unwillingness to foreclose an argument, and by extension a possible development of the law, that an express assignment or assumption of contractual obligations without recourse to the transferor is effective under certain circumstances. Such a path of exploration may no longer run counter to orthodoxy; for instance, Andrew Smith J. has signalled extrajudicially that established doctrines about transferring burdens should require fresh examination.<sup>64</sup> At present, English law generally permits one to assign only rights and not burdens under a contract.<sup>65</sup> Allowing obligations to be expressly assigned with (or without) the consent of the obligee would move it closer to some Continental legal systems.<sup>66</sup> But clearly any question of modification or abolition of the English rules on assignments of burdens will require careful consideration.

<sup>62</sup> *Omar v El-Wakil* [2001] EWCA Civ 1090, [2002] 2 P. & C.R. 3, at [33] (Arden L.J.); contra *Cave v Robinson Jarvis & Rolf* [2001] EWCA Civ 245, [2002] 1 W.L.R. 581, at [28] (Potter L.J.), [37] (Jonathan Parker L.J.) (on appeal the House of Lords did not hear or rule on arguments on the question of precedent: [2002] UKHL 18, [2003] 1 A.C. 384, at [66] (Lord Scott of Foscote)). The fact of the application’s having been fully argued may not change the (non-)binding nature of the resulting decision: *MY (Pakistan) v Secretary of State of the Home Department* [2021] EWCA Civ 1500, [2022] 1 W.L.R. 238, at [17] (Underhill L.J.). This is not the only issue of *stare decisis* afflicting the Court of Appeal: see K.H. Lau, “High Court Masters and the Upper Tribunal” (2021) 40 C.J.Q. 249, 255, n. 38.

<sup>63</sup> See also J. Little, “Novation of Contractual Obligations: A Joint Venture Perspective” [2005] AMPLA Yearbook 98, 109. The unaddressed difficulty here would have been that the phrase “assignment, assumption and release” that was used in the relevant clause was terminology more commonly found in contracts governed by US law (as the court was informed): *Graiseley Properties v Barclays Bank* [2013] EWCA Civ 1372, at [36]. Transposing that into English law might result in one of at least four alternative outcomes: that the operative language was ineffective to transfer any obligations; that it was effective to assign both rights and obligations; that it was effective to assign rights and novate obligations; or that it was effective to novate both rights and obligations. In the last possibility, it might then also be debatable whether the new party took subject to equities affecting the outgoing party.

<sup>64</sup> “Foreword”, in M. Smith, *The Law of Assignment* (Oxford 2007), v. See elsewhere *Circuit-Systems Ltd. v Zuken-Redac (UK) Ltd.* [1997] 1 W.L.R. 721, 732 (Staughton L.J.); *Promontoria (Henrico) Ltd. v Samra* [2019] EWHC 2327 (Ch), [2019] C.T.L.C. 295, at [88] (H.H.J. David Cooke); Lau, “Unilateral Transfers of Contractual Obligations”, 491–92.

<sup>65</sup> In the syndicated loan context, see Bridge et al., *Law of Personal Property*, [25–008].

<sup>66</sup> Cf. S. Woyciechowski, “Transfer of Contract” in N. Jansen and R. Zimmermann (eds.), *Commentaries on European Contract Laws* (Oxford 2018), 1753.

Another puzzle is the splintering contract, one best illustrated with an example. Take again the hypothetical involving the borrower, Bank *X* and Bank *Y*, but with the following twist: at a meeting prior to the execution of the facility agreement, authorised representatives of each bank committed actionable misrepresentation in rendering factually inaccurate advice to the borrower, who relied upon that advice in entering into the agreement. After the agreement is executed but before draw-down of the principal sum, Bank *X* sells its £5 million share of the loan to Bank *Z* on the secondary market, and they also follow the novation procedure prescribed in the facility agreement similar to what was done in *Argo Fund*, thereby eliminating the active participation of both Bank *Y* and the borrower in the novation. The borrower later discovers the inaccuracy of the advice it received from the representatives of Banks *X* and *Y*.

If one accepts the existence of the concept of partial novation as adumbrated in *Deutsche Bank* then it may be that the borrower could mount a claim for rescission against Bank *Y*, but not against Banks *X* and *Z*. Bank *X* escapes because one outcome of the novation was to end its contractual relations altogether with the borrower, while Bank *Z* escapes because it has entered into a fresh contract with the borrower *sans* right to rescind. Bank *Y*, on the other hand, remains a party to the original facility agreement, bound by any equities<sup>67</sup> attaching thereto, because it did not actively participate in the novation process effected among the borrower, Bank *X* and Bank *Z*. What has supposedly happened in literal and figurative silence during that process is the splintering of the original agreement among the borrower, Bank *X* and Bank *Y* into three contracts after the novation: one between the borrower and Bank *Y* (which is the original agreement with equities between them remaining unextinguished); one between the borrower and Bank *Z* (a new contract without any equities attaching that relate to the original agreement); and one between Banks *Y* and *Z* (also a new contract without any equities attaching which relate to the original agreement).<sup>68</sup> Together these constitute the post-novation contractual relationship among the borrower, Bank *Y* and Bank *Z*.<sup>69</sup>

The creeping feeling of unreality about this analysis probably stems from its complexity and how divorced it seems from the likely contracting intention behind the use of an “advance consent” provision to streamline the process of novation.<sup>70</sup> Parties harnessing the words “novation of the contract”

<sup>67</sup> In this example the equity is a right to rescind, but other equities conceivably exist such as a right of set-off.

<sup>68</sup> See also the understanding of partial novation in *Bailey v Barclays Bank* [2014] EWHC 2882 (QB), at [70] (H.H.J. Keyser Q.C.).

<sup>69</sup> A similar type of splintering was thought to have possibly occurred in *Langston Group Corp v Cardiff City Football Club* [2008] EWHC 535 (Ch), discussed above.

<sup>70</sup> In practice it is common for novation scenarios to feature more parties than are present in the hypothetical situation. The *Deutsche Bank* case, for instance, saw nine separate lenders becoming privy to a credit facility agreement at different junctures. In *Redwood Master Fund Ltd. v TD Bank Europe Ltd.*

(or words to those effect) in their agreements, particularly commercial agreements, should generally be taken to understand that that involves the discharge of the original contract and the creation of a new contract for all of the parties concerned,<sup>71</sup> unless the context clearly reveals otherwise.<sup>72</sup> But the introduction of the concept of partial novation here would heavily qualify that understanding and invent a *tertium quid*.<sup>73</sup> If a party like Bank *Y* or the borrower, having given its consent in advance to a novation of a contract, does not then actively participate in the actual novation, it may be bound by the original contract which is not fully discharged so far as that party is concerned. That is simply unlikely to reflect the position envisioned at the outset, especially so if the parties theoretically could, in lieu of utilising the “advance consent” mechanism, have come together always to conclude a separate agreement for novation, in which case it would be beyond reasonable dispute that prior equities had not become attached to the new contract.<sup>74</sup> Lastly, there will be obvious challenges in maintaining and substantiating a concern to preserve equities attaching to the original contract – a concern that moved the court in *Deutsche Bank*<sup>75</sup> – in the face of a stipulation inserted by the parties dictating the non-survival of equities following any novation.<sup>76</sup>

Given the intricate interplay of doctrine and practice surrounding the resolution of these questions, Longmore L.J. was, with respect, surely

[2002] EWHC 2703 (Ch), [2006] 1 B.C.L.C. 149 there were more than 46 lenders at the relevant time. The possibility of a partial novation in these scenarios may appear somewhat incredible.

<sup>71</sup> In *Habibsons Bank v Standard Chartered Bank* [2010] EWCA Civ 1335, at [23], Moore-Bick L.J. observed that the standing offer would have been made by the borrower to all the lenders and *could not have been revoked without the consent of all of them*.

<sup>72</sup> Burton J. in *CMA CGM S.A. v Hyundai Mipo Dockyard Co. Ltd.* [2008] EWHC 2791 (Comm), [2009] 1 Lloyd’s Rep. 213, at [23] seemed to incline to the view that a substitution of one obligor for another which was described by the parties as a “novation” might not have the effect of extinguishing the original contract and creating a new contract, but operate simply to “repeople the original contracts, leaving their provisions (including their dates) unchanged”. Some commentators have generously interpreted the passage to mean that this “repeopling” remains a novation, albeit that the *extent* of novation is flexible and dependent on the intention of the parties: Bridge et al., *Law of Personal Property*, [25-010–25-011]. On novation and variation, see also *Samuels Finance Group plc v Beechmanor Ltd.* (1994) 67 P. & C.R. 282, 285 (Lloyd L.J.); *Telewest Communications plc v Customs and Excise Commissioners* [2003] EWHC 3176 (Ch), [2004] S.T.C. 517, at [57] (Sir Francis Ferris); [2005] EWCA Civ 102, [2005] S.T.C. 481, at [26] (Sir Christopher Staughton); *Musst Holdings Ltd. v Astra Asset Management UK Ltd.* [2021] EWHC 3432 (Ch), at [392] (Freedman J.); *ALH Group Property Holdings Pty. Ltd. v Chief Commissioner of State Revenue of the State of New South Wales* [2012] HCA 6, (2012) 245 C.L.R. 338; L.C. Ho, “Novation, Variation and Rescission: A Question of Intention?” (2008) 1 Corporate Rescue and Insolvency 95, 96.

<sup>73</sup> Elsewhere described as a “novation with ‘assignment-like’ features”: Gullifer and Payne, *Corporate Finance Law*, 464.

<sup>74</sup> Of course, this does not mean that the parties cannot agree, in their agreement to novate, that certain equities between some or all of them are to be preserved (for instance, by providing that the novation be on the same terms as the original contract immediately prior to the effective time of the novation), but the point is that it would require an express act to *move away* from the (present) default position that a novation results in a new contract without prior equities attaching to it.

<sup>75</sup> See also Bailey, “Novation”, 204, n. 78.

<sup>76</sup> In light of the complexity of the case, it was perhaps a relief (and no doubt a disappointment to some legal academics) that the court in *Deutsche Bank* did not have to contend with any such stipulation. See also M.J. Smith, “Transmitting the Benefit of a Letter of Credit” [1991] J.B.L. 447, 449–50; Little, “Novation of Contractual Obligations”, 107.

correct that the concept of partial novation should be judicially introduced into English law (if at all) only after a substantive hearing with the benefit of detailed argument. The view offered here is that the common law should either modify or jettison the existing understanding of partial novation, to the extent that that contemplates the splintering of a contract following novation of the entirety of the contract. Any residual anxiety that obligors then become free to evade their liabilities or obligations in a way that improperly defeats a legitimate interest or expectation is more appropriately ameliorated using the protective devices shortly to be discussed.

#### *D. Protection*

It is suggested that, in evaluating the use of an “advance consent” term for a future novation, an allied task must be the devising of suitable legal controls to mitigate the risks of obligors abusing that mechanism to unfairly discard their liabilities, as well as the risks faced by obligees in being inappropriately exposed to the consequences of non-performance of obligations. And yet the contemporary judicial instinct might fairly be summarised as one that upholds “advance consent” provisions with minimal curial interference. In recent memory there has been one occasion in the English courts where protection was expressly mooted for the hapless obligee. That arrived in the form of an obiter dictum in *Argo Fund*, where Rix L.J. remarked that an obligor who deliberately “shuffle[d] off” its contractual obligations to a third party that was not capable of fulfilling them might breach an implied term to the effect of a warranty that the third party was capable of performing them.<sup>77</sup>

##### *1. Common law implication*

The untested character of Rix L.J.’s proposed limitation ought not to diminish its attraction of simplicity. Viewing the restriction upon an obligor’s exercise of the right to novate through the lens of implication would require only adaptation of familiar principles of law. The implied term could be cast as a warranty by the obligor (in favour of the obligee) that it does not have reasonable grounds to know of the novatee’s inability or unwillingness to perform the novated obligations. That formulation develops Rix L.J.’s dictum but employs a test of reasonableness in place of any absolute standard of knowledge, to accommodate English law’s general dispensation regarding perfect foresight as well as its acceptance of damages to be an adequate substitute for performance in most cases.

In addition, a threshold of reasonableness would be preferable to allow the circumstances of individual cases to be considered in their proper

<sup>77</sup> *Argo Fund v Essar Steel* [2006] EWCA Civ 241, at [70].

context. In *British Gas Trading Ltd. v Eastern Electricity plc*,<sup>78</sup> a term in the contract stated that the obligee's approval of a novation was not to be unreasonably withheld. Colman J. found that the main purpose of that term, construed in the light of the other contractual provisions, was to enable the obligee to investigate and ascertain the ability and willingness of any proposed novatee to perform the contract post-novation. Since it was accepted that the prospective novatee there *did* have the financial status and ability to observe and perform the transferred obligations, the obligee could not have reasonably withheld its approval of the novation; it might have been otherwise if there were evidence of a material risk or possibility of the novatee's inability or unwillingness to perform the contract (which was not the case). The Court of Appeal upheld the judge's ruling.

*British Gas Trading* was primarily about the interpretation of a specific clause, but that decision also evidences the court's desire to want to consider the nature and circumstances of the transaction when determining the issue of consent to novation. The judicial examination ought *not* to descend to second-guessing the intentions of parties, who should not fear unduly triggering a breach of the implied term so long as they act in accordance with ordinary standards of (commercial) behaviour. Usage of "advance consent" terms is now widespread in facilitating value exchanges, sometimes involving very significant amounts as in secondary market transactions. The courts should conduct their scrutiny against this backcloth.

Considerations of policy, fairness and reasonableness, which are relevant to the implication of a term in law,<sup>79</sup> suggest that the warranty if introduced could operate by default in any contract containing an "advance consent" provision. Few would be heard to contend for an obligor to be allowed to shed its liabilities to a person it had reasonable basis to know could not discharge them. In certain circumstances, perhaps, the implied term might be contractually excludable, which should require at least express words or a necessary implication.<sup>80</sup> One common attempt is to insert an entire agreement clause but that would need to contain clear and adequate wording to successfully perform the exclusionary function.<sup>81</sup> A possible exclusion by necessary implication might be where, at the obligee's request, the class of potential novatees was limited to those persons having fiscal strength (e.g. based on specified financial ratios) sufficient in the ordinary course of business to perform the obligor's contractual obligations.

<sup>78</sup> Unreported, QBD, 19 November 1996; CA, 18 December 1996.

<sup>79</sup> *Crossley v Faithful & Gould Holdings Ltd.* [2004] EWCA Civ 293, [2004] 4 All E.R. 447, at [36] (Dyson L.J.); *Geys v Société Générale, London Branch* [2012] UKSC 63, [2013] 1 A.C. 523, at [56] (Baroness Hale J.S.C.).

<sup>80</sup> *Johnson v Unisys Ltd.* [2001] UKHL 13, [2003] 1 A.C. 518, at [24] (Lord Steyn).

<sup>81</sup> *Mathews v Kuwait Bechtel Corporation* [1959] 2 Q.B. 57, 63 (Sellers L.J.); *Ranson v Customer Systems plc* [2012] EWCA Civ 841, [2012] I.R.L.R. 769, at [63] (Lewison L.J.); *Nigeria v JP Morgan Chase Bank NA* [2019] EWHC 347 (Comm), [2019] 1 C.L.C. 207, at [37] (Andrew Burrows Q.C.) (aff'd. [2019] EWCA Civ 1641, [2019] 2 C.L.C. 559, at [40] (Rose L.J.)).



To summarise, then, a term could be implied in respect of the obligor's exercise of its right to novate, possibly framed as a warranty given by the obligor in favour of the obligee that it does not have reasonable grounds to know of the novatee's inability or unwillingness to perform the obligations so novated. Breach of the term, if not excluded, should ordinarily result in some compensation moving from the obligor to the obligee if the latter suffers loss following the novatee's (non-)performance under the new contract. It does not mean that the obligor will inevitably bear liability for the novatee's defective performance or that the obligor must make compensation to the same order as what the novatee would be liable for. The determination should focus on whether the obligor had reasonable grounds to know of the novatee's inability or unwillingness to perform and, if so, the extent to which the resulting loss is properly shouldered by the obligor. Such an apportionment of liability would be an exercise not unfamiliar to the courts.

## *2. Equitable limitations*

There are, however, limits to the ways an implied term can address the problem of abuse. It may not be able to prevent a determined obligor from using the fact of novation to erase from existence the obligee's rights against the obligor – such as a right to set-off, rescind or terminate – primarily because breach of the implied term would not have the effect of invalidating the novation itself.<sup>82</sup> An alternative approach to risk mitigation would rely upon use of equitable principles and propose that any novation effected pursuant to an “advance consent” term has to be carried out honestly and in good faith, and, as one corollary of that principle, that it cannot be done to allow the obligor to get rid of its liabilities unfairly or improperly. Authority for these prescriptions arrives, somewhat surprisingly, in the form of a spate of decisions emanating from the collapse of numerous life assurance companies in the nineteenth century.

The Royal Naval, Military and East India Company Life Assurance Society (RNS) was an unincorporated company with which one Mr. Hort had, in each of 1855 and 1857, taken out an assurance policy on his life. The policy terms provided that, upon payment of the stipulated premiums, the capital, stock and funds of the company would “according and subject to the provisions of the [company's] deed of settlement” be liable to pay out the assured sums upon satisfactory proof of death. A clause in the company's deed of settlement allowed its directors, upon dissolution of the company, to transfer its funds and property to another assurance company or society to enable that other company or society to pay or satisfy any future claims or demands that might otherwise have been made on the

<sup>82</sup> I am grateful to the Editor, Louise Gullifer, for prompting thought on this point.



dissolved company. RNS was dissolved in 1866 and a part of its property and assets transferred to the European Assurance Society (EAS). At the same time EAS and its directors covenanted that it, and its property and assets, should pay and satisfy all future liabilities on life or annuity policies that had already been issued by RNS. Mr. Hort was alive at the time of this transfer. In fact he was still alive when orders were made in 1872 for the winding up of EAS as well as RNS. Not unexpectedly, he made a claim in respect of his policies against the latter. Lord Westbury adjudged Mr. Hort entitled to prove on both his policies against RNS. That decision was appealed and a special case thereafter stated for the opinion of the Court of Appeal in Chancery.

Differing from Lord Westbury, the court held unanimously that, on its ordinary and true construction, the deed of settlement gave RNS the right to transfer its assets and liabilities, without the consent of the policyholders, to another assurance company or society.<sup>83</sup> To this Mr. Hort had agreed when he accepted the two policies taken out on his life.<sup>84</sup> One of the judges (Lord Cairns L.C.) was of the further opinion that Mr. Hort had had clear notice of the arrangements being undertaken by the two assurance companies and could not have objected to them.<sup>85</sup> Notably, both the Lord Chancellor and James L.J. insisted that Mr. Hort's case was not about novation but simply one of the construction of a contract.<sup>86</sup> The claim appears implausible in light of their finding that it was the liability on the very same policies issued by RNS that the incoming assurance company (i.e. EAS) was obliged to assume after the transfer in 1866, and that the former company had thereafter ceased to carry on business and was dissolved as far as could properly have been done – meaning that there was no longer any effective recourse to the original party.<sup>87</sup> At the time no technique (such

<sup>83</sup> *In re European Assurance Society (Hort's Case)* (1875) 1 Ch. D. 307, 319–22.

<sup>84</sup> In a later, unrelated decision, the Court of Appeal reached the same conclusion in respect of a policy which did *not* expressly refer to the company's deed of settlement, because the circumstances there revealed that the policy must have impliedly meant that the company's funds were liable according to the deed of settlement: *In re European Assurance Society (Dowse's Case)* (1876) 3 Ch. D. 384, 387 (James L.J.).

<sup>85</sup> *In re European Assurance Society (Hort's Case)* (1875) 1 Ch. D. 307, 319–20. Interestingly, in the later case of *In re European Assurance Society Arbitration Acts and Industrial and General Life Assurance and Deposit Co. (Cocker's Case)* (1876) 3 Ch. D. 1, 9–10, Lord Cairns L.C. thought that a policyholder might, after being notified of the proposed transfer, be able to raise an objection thereto despite having initially consented through acceptance of the policy and deed of settlement. His earlier view seems preferable, not only because it would be relatively simple for parties to draft their contracts in such a way as to get around the notification-and-consent requirement, but more importantly because that requirement gives the obligee a second bite at the cherry, so to speak, when *ex hypothesi* it would already have executed a contract in which it ostensibly consented to a future novation.

<sup>86</sup> *Ibid.*, at 319 (Lord Cairns L.C.) and 322 (James L.J.); cf. Mellish L.J.'s views at 323. See also the reluctance to use the term "novation" in *In re European Assurance Society (Harman's Case)* (1875) 1 Ch. D. 326, 332 (Lord Cairns L.C.).

<sup>87</sup> Lord Cairns L.C. had in fact characterised Mr. Hort's policy of assurance as one which was "in its nature open to the chance of shifting": *In re European Assurance Society (Hort's Case)* (1875) 1 Ch. D. 307, 319.

as delegated or substituted performance) apart from novation could have achieved those precise results.<sup>88</sup>

Several additional matters should be noted. Clearly the nature of the contract in question heavily influenced the outcome. Here was an assurance policy taken out with a company which could conceivably subsist for many years after its issuance. Lord Cairns L.C. observed that there was “considerable reason” why the company might wish to provide in its deed of settlement for some sort of arrangement by which its business was transferrable to another entity; there was otherwise no practical mode by which insurance companies could come to an end.<sup>89</sup> So much for the interests of the company, but the interests of the policyholders were also not neglected. According to James L.J. there were benefits that would accrue to them in allowing an insurance company to transfer its assets, liabilities and business to another company:

[If] a sufficient amount of business is not obtained to begin with, or if the business falls off, so that the assets and the probable future income of the society will not be sufficient to provide amply for all the liabilities which it has entered into and is entering into, the honest and proper course is to get some larger, stronger, and more prosperous society to accept the liabilities of the unprosperous society which, out of its assets, would pay a sufficient sum to induce the more prosperous society so to do . . . Therefore it is not that there is anything wrong in the provisions, because it was a reasonable and proper provision to make for the safety, not only of the shareholders, but of the persons insured.<sup>90</sup>

It is unsurprising that the interests of policyholders should have featured on the judges’ minds as they examined the provision purportedly allowing the assurance company to transfer its liabilities, including those arising from policies already issued, to another assurance company without the consent of the holders. The atmosphere surrounding the massive insolvencies of life assurance companies was febrile, and the claim was also being heard in a court of equity.<sup>91</sup>

<sup>88</sup> Even today, saying that the substitution of a party is not a novation because the substituting party performs the original contract comes very close to an analysis Davis L.J. mooted in *Budana v Leeds Teaching Hospitals NHS Trust* [2017] EWCA Civ 1980, [2018] 1 W.L.R. 1965, at [93], [102] but which was rejected by his colleagues. The majority, disagreeing with Davis L.J., preferred a novation-based analysis: at [65]–[69] (Gloster L.J.), [118]–[119] (Beaton L.J.). For another view, see *Weyerhaeuser v Hayes* 2008 BCCA 69, at [19]–[25] (Low J.). Approaching the matter along the lines of novation (instead of performance) suggests that we should properly distinguish substitutions from variations where one party consents to the other’s having the right to unilaterally amend the terms of their contract (subject to legislation such as the Consumer Rights Act 2015, s. 63, read with Schedule 2, paragraphs 11, 22, 23, 24): see *Wandsworth London Borough Council v D’Silva* [1998] I.R.L.R. 193, at [31] (Lord Woolf M.R.); *Bateman v Asda Stores Ltd.* [2010] I.R.L.R. 370, at [31] (Silber J.); *Amberley (UK) Ltd. v West Sussex County Council* [2011] EWCA Civ 11, at [22] (Aikens L.J.); *MPloy Group Ltd. v Denso Manufacturing UK Ltd.* [2014] EWHC 2992 (Comm), at [65] (Christopher Butcher Q.C.).

<sup>89</sup> *In re European Assurance Society (Hort’s Case)* (1875) 1 Ch. D. 307, 317–18.

<sup>90</sup> *Ibid.*, at 321. He would repeat a similar view in *In re European Assurance Society Arbitration Acts (Doman’s Case)* (1876) 3 Ch. D. 21, 27.

<sup>91</sup> This was due to the winding up and the interposition of trusts law in the constitution of the unincorporated companies. For more on this historical business form, see R. Harris, *Industrializing English Law*:

This period of upheaval hints at what can go wrong with the advance consent proposition and at the types of guardrails required to be installed around it. Indeed, the judgments in Mr. Hort's case and in other contemporary decisions classically dictate certain limitations on one's ability to unilaterally carry out a transfer, even if a contractual provision might exist for that purpose at its favourable option. According to them, any transfer has to follow literally and properly the mechanism set out within that provision;<sup>92</sup> it has to be carried out honestly and in good faith;<sup>93</sup> and it cannot be undertaken to allow the transferring entity to get rid of its liabilities unfairly or improperly.<sup>94</sup> It is difficult to define these limits with greater specificity without circumscribing the court's ability to remedy injustice,<sup>95</sup> a task that can benefit from equity's ranging methods of inquiry, although care should be taken generally to avoid hindsight and to account for the circumstances and state of knowledge available at the time of the purported novation. Equitable relief should follow any contravention of the limitations, subject to the usual bars.<sup>96</sup>

Contrasted with the common law implication of a warranty, a proper application of these equitable limitations may offer fuller protection while affording the courts greater latitude to take relevant commercial considerations into account. Had the facts of *Argo Fund* or *Habibsons Bank* been viewed through the prism of equity, for instance, it would have been clear that none of the transfers were impugnable on the ground that the transferor was acting in bad faith or getting rid of a liability in an improper

*Entrepreneurship and Business Organization, 1720–1844* (Cambridge 2000), chapter 6; J. Morley, "The Common Law Corporation: The Power of the Trust in Anglo-American Business History" (2016) 116 *Colum. L. Rev.* 2145; J.D. Turner, "The Development of English Company Law Before 1900" in H. Wells (ed.), *Research Handbook on the History of Corporate and Company Law* (Cheltenham 2018).

<sup>92</sup> *In re European Assurance Society (Hort's Case)* (1875) 1 Ch. D. 307, 318 (Lord Cairns L.C.).

<sup>93</sup> *In re The Times Life Assurance and Guarantee Co., ex parte Nunneley* (1870) 39 L.J. Ch. 297, 302 (James V.C.) (affd. (1870) 39 L.J. Ch. 527); *In re European Assurance Society (Hort's Case)* (1875) 1 Ch. D. 307, 318 (Lord Cairns L.C.); *In re European Assurance Society Arbitration Acts and Industrial and General Life Assurance and Deposit Co. (Cocker's Case)* (1876) 3 Ch. D. 1, 9 (Lord Cairns L.C.); *In re European Assurance Society Arbitration Acts (Doman's Case)* (1876) 3 Ch. D. 21, 26 (Lord Cairns L.C.) and 27 (James L.J.). It might separately be contended that the exercise of the right to novate involves the exercise of a type of inherent discretion on the part of the obligor, thereby drawing into play the regulating duties enunciated in *Braganza v BP Shipping Ltd.* [2015] UKSC 17, [2015] 1 W.L.R. 1661. Later cases do not appear (yet) to have endorsed such a proposition, at least in respect of an absolute right to novate. Assuming the existence of the equitable jurisdiction as developed in this article, however, there may be less urgency to determine the correctness or suitability of *Braganza* so far as relates to a clause that confers a right to novate (or assign).

<sup>94</sup> *In re European Assurance Society (Hort's Case)* (1875) 1 Ch. D. 307, 318 (Lord Cairns L.C.); *In re European Assurance Society Arbitration Acts (Doman's Case)* (1876) 3 Ch. D. 21, 26 (Lord Cairns L.C.). It may incidentally be noted that Mellish L.J., without having to decide the question in *In re European Assurance Society (Harman's Case)* (1875) 1 Ch. D. 326, 333, mused over whether a provision which merely permitted a company to undertake a sale or amalgamation without the consent of the policyholders would be sufficient to enable the shareholders to get rid of their liabilities.

<sup>95</sup> Comparisons to insolvency legislation may be helpful although caution should be exercised owing to the specific context of such legislation.

<sup>96</sup> *In re The Times Life Assurance and Guarantee Co., ex parte Nunneley* (1870) 39 L.J. Ch. 297, 302 (James V.C.).

manner. In each case the selling bank was simply transacting in the secondary market as an ordinary participant would. If, hypothetically, the selling bank had had an unexhausted obligation to lend to the borrower and that obligation was effectively transferred to the purchasing bank or financial institution, a court would have to look at the entire context and circumstances surrounding the transfer in determining whether to set it aside for impropriety. In this relation there can and should be no presumption that a transfer is an evasive manoeuvre; what is important is that parties adhere to ordinary standards of commercial fair dealing. Finally, it also means that Cooke J.'s unvoiced concern in *Habibsons Bank*, mentioned earlier, that the efficacy of an "advance consent" term could be put in question if the obligation to be novated had not been fulfilled at the point of novation, is both valid and well handled: equity can provide a means by which legitimate transfers are set apart, with due care and commercial sensitivity, from those that are illegitimate.

## V. CONCLUSION

Where does this leave the issue of advance consent to novation? It appears that the balance lies in accepting that people should be able to provide their advance consent to a future novation, but without having to give the transferring party *carte blanche* in every respect. And it is preferable to concede that there is great commercial advantage *and* potential injustice in recognising a theory of advance consent to novation. Given how the modern authorities do not fully consider the risks and possible methods of abuse, the conclusions of this article are summarised by using the example set out at the beginning.

Suppose *A* and *B* are looking to contract with each other. *B* wishes to introduce an "advance consent" term by which *A* provides its consent to a possible novation of the contract from *B* to an unknown third party in the future. *A*'s first line of defence is either to reject that entirely or to negotiate for the term to be framed such that its consent becomes a conditional one. Some common conditions are that any future novation should take place within or not before a certain time; that the potential novatee should fall within a prescribed class (such as a person who is related to or affiliated with *B* or who meets certain qualifications);<sup>97</sup> or that prior notice of the novation and the novatee's identity should be given to *A* (who might or might not have a right to reject the novation, possibly to be exercised within a predetermined duration). Yet other conditions may be imposed and if so they should be sufficiently clear and certain for their fulfilment to be

<sup>97</sup> Rawlings, "Restrictions on the Transfer of Rights in Loan Contracts", 544; S. McCracken et al., *Everett and McCracken's Banking and Financial Institutions Law*, 9th ed. (Pymont, NSW. 2017), [15.410]; G. Penn, "Promoting Liquidity in the Secondary Loan Market: Is Sub-participation Still Fit for Purpose?" (2022) 37 J.I.B.L.R. 85, 99–101.

objectively ascertained. As *Argo Fund* and *Habibsons Bank* indicate, the term itself must then at least contain a formal mechanism to be followed by the relevant parties, one which is not nebulous and whose fulfilment is also capable of objective ascertainment, and provide sufficient certainty as to the terms of the new contract that is subsequently formed between *A* and the novatee, *C*, after the novation. (It should also address the post-novation status of equities between the parties, if they desire greater certainty on issues relating to partial novation.<sup>98</sup>)

Should an “advance consent” term become part of the contract between *A* and *B*, a future novation may permissibly be effected by *B* in accordance with that term and without needing *A*’s specific consent to the novation if the term so allows and if *A*’s advance consent has not been withdrawn.<sup>99</sup> This is also subject to operative statutory limits.<sup>100</sup> Any conditions as well as the formal mechanism in respect of the novation has to be literally and properly fulfilled and followed. Assuming that waiver and estoppel do not apply, a failure to observe the prescribed provisions generally renders the purported novation legally ineffective, with the original contract between *A* and *B* remaining afoot and no new contract coming into existence between *A* and the purported novatee.

To mitigate the risks of abuse and non-performance inherent in the advance consent proposition, one of two alternative approaches might be adopted. The first is equitable in nature and to say that any novation effected pursuant to the “advance consent” term is subject to the limitations first derived from the life assurance cases. The other is to be found in the common law implication of a warranty given by *B* in favour of *A* that it does not have reasonable grounds to know of *C*’s inability or unwillingness to perform the novated obligations. As between the two approaches, one can contend that the equitable approach more authoritatively represents the state of English law at present. But the antiquity of the line of cases it relies upon means that the area is ripe for re-examination on principle to produce a clearer, updated set of rules for modern application. It is worth repeating that a proper appreciation of the context will necessarily have to inform any judicial scrutiny. “Advance consent” terms are in common circulation and, in cases where ordinary standards of (commercial) behaviour are met, the courts should not readily question or go behind the apparent motives behind the usage of such terms. So, for example, banks and financial

<sup>98</sup> See Goode and Gullifer, *Goode and Gullifer on Legal Problems of Credit and Security*, [3-10], n. 72. Ultimately the terms of the new contract following novation can be moulded by agreement, including in relation to the survival of rights and equities. It is not inconceivable that formal recognition of a concept of partial novation (as described in the pages above) will provoke a drafting response to the effect that, following a novation among some or all of the parties, any equity attaching in respect of the contract immediately prior to the novation is extinguished save as otherwise agreed.

<sup>99</sup> On the withdrawal of consent, see Bridge et al., *Law of Personal Property*, [25-005].

<sup>100</sup> See e.g. Consumer Rights Act 2015, s. 63, read with Schedule 2, paragraph 7.

institutions should continue to be able to legitimately trade loan assets, and companies able to pursue restructuring and consolidation exercises.

Whichever approach is selected, it is suggested that the curially imposed limitations on the operation of the advance consent proposition should generally apply in every contracting context. That has the advantage of eschewing entangled inquiries when applying the advance consent proposition in practice, inquiries that might otherwise require one to differentiate, for instance, between contracts entered into with consumers and with non-consumers, or between long-term and short-term contracts. More broadly, a universal approach would maximise the permissive and restrictive aspects of the advance consent proposition: to allow the commercial advantages of the proposition to be generally realisable for all, but also to establish a consistent form of protection against improper and dishonest behaviour.