

# Insight: Derivatives

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## ISDA Master Agreement choice of English Jurisdiction upheld

In the recent case of *Berliner Verkehrsbetriebe (BVG) Anstalt Des Offentlichen Rechts v JP Morgan Chase Bank N.A., JP Morgan Securities Limited* [2010] EWCA Civ 309, Berliner (a German public body) has entered into a credit default swap with JPMorgan. The ISDA Master Agreement conferred exclusive jurisdiction on the English courts.

Following the occurrence of certain credit events, JPMorgan sought payment under the credit default swap in proceedings commenced in England. Berliner responded by suing JPMorgan in Germany claiming that its board decisions to enter into the credit default swap were *ultra vires* as a matter of German law. Berliner also challenged the jurisdiction of the English courts on the basis of the provisions of Article 22(2) and Article 25 of Council Regulation (EC) No 44/2001 (the "**Regulation**"). For convenience, these Articles are set out in full in the annex hereto.

At first instance, Teare J had held that the English courts had jurisdiction because the subject proceedings were not "*overall*" principally connected with matters that fell within Article 22(2) of the Regulation and that the parties should be held to their contractual agreement that the English courts had jurisdiction. The first instance decision was appealed by Berliner to the Court of Appeal.

Lord Justice Aikens summarised the background to the appeal as follows:

- "1 *Credit default swap arrangements are giving rise to litigation again. As is so often the case in commercial disputes, the first battle is over jurisdiction. In this case, the battle is whether the English court should have jurisdiction, as the parties agreed in their contractual arrangements, or whether the Berlin Landgericht (or Berlin Regional Court) should have jurisdiction, pursuant to the provisions of Article 22.2 and Article 25 of Council Regulation (EC) No 44/2001; viz. the Jurisdiction and Judgments Regulation ("the Regulation"). Teare J held, in his judgment of 9 July 2009, that the English court had jurisdiction, because the proceedings before the Commercial Court were not "overall" principally concerned with matters that fell within Article 22.2 of the Regulation. Therefore, because the parties had agreed that the English court should have jurisdiction, they should be held to that agreement, pursuant to Article 23 of the Regulation.*
- 2 *The judge gave permission to appeal... The appeal raises interesting points on the scope and application of Article 22.2 of the Regulation, in particular when proceedings involve multiple issues of which one, at least, falls within the ambit of Article 22.2 of the Regulation and has the potential to be dispositive of the entire proceedings.*



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4 *The credit swap arrangement which gives rise to the litigation is called an “Independent Collateral Enhancement Transaction” or “ICE Transaction.” It was considered at a series of meetings between JPM and BVG management which took place between July 2006 and June 2007. BVG resolved to enter into the ICE Transaction by resolutions of its Management Board in March 2007 and its Supervisory Board in April 2007. It is BVG’s contention in the present dispute that those decisions of the Management and Supervisory Boards were ultra vires and therefore void and that this means that the subsequent contracts for the credit default swap arrangements are void. It is common ground that the issue of whether any decisions of the Management and Supervisory Boards were ultra vires has to be dealt with according to German law. BVG also contends that in the meetings between its management and JPM representatives, BVG was given incorrect advice about the ICE transaction and its effect.*

8 *Following the turmoil in the financial markets both before and after the collapse of Lehman Brothers on 15 September 2008, seven out of the 150 credit risks (including Lehman Brothers Holdings Inc and three Icelandic banks) have materialised. As a result, in the present proceedings JPM now claims US\$ 112 million from BVG under the terms of the JPM Swap.<sup>1</sup>*

10 *... It was common ground before the judge and before us that the terms of the first declaration sought by JPM in the English proceedings would encompass issues of the vires of decisions of the Management and Supervisory Boards of BVG to enter into the JPM Swap.*

31 *Both parties accept that the English proceedings raise a number of issues, including the issue of whether the decisions taken by BVG’s management and supervisory boards were ultra vires so as to make void or invalidate the contracts for the JPM Swap. It is also common ground that if Article 22.2 applies to the English proceedings, then the English court will be obliged, in accordance with Article 25 of the Regulation, to declare that it has no jurisdiction to entertain the current English proceedings.*

32 *Therefore, in my view, the focus of this appeal must be on Article 22.2, although it is clear that the correct interpretation of Article 22.2 is also going to involve consideration of the interpretation of the words “principally concerned with” in Article 25. Therefore I think that the two principal issues we have to decide are: (1) what is the correct interpretation of Article 22.2; and (2) how are the facts of this case to be applied to the correct interpretation of Article 22.2 and Article 25?”*

### Correct Interpretation of Article 22(2)

After an exhaustive review of the relevant authorities and background commentary to the Regulation, Lord Justice Aikens held as follows:

“83 *The proper interpretation of Article 22.2 has to be derived from its wording, its objective, its position in the scheme of the Regulation, the ECJ decisions on Article 22 and its predecessor, the commentary of Mr Jenard and the English cases on the Article. My conclusions on its interpretation are as follows: first, I think we are bound by English Court of Appeal authority to interpret*

*the words “... proceedings which have as their object...” in Article 22.2 as “proceedings which are principally concerned with”.*

87 *...given my view that the Court of Appeal in the Grupo Torras<sup>2</sup> case did endorse the approach of Mance J that a court has to undertake an exercise in “overall classification” and make an “overall judgment” to see whether the proceedings are “principally concerned” with one of the matters set out in Article 22.2, we are bound to follow that interpretation unless there has been a subsequent decision of the ECJ (or House of Lords) which has stated a contrary interpretation. There is none.*

88 *In any case, in my respectful view the interpretation of Mance J was correct. It fits with the wording of Article 25. It also fits with the objective of Article 22, which is to give exclusive jurisdiction to the courts of the state which will be best suited to dealing with the relevant issue, depending on which paragraph of Article 22 is in play. It is only necessary to displace the general rule as to jurisdiction or the parties’ own agreed jurisdictional choice if, making an overall judgment, it is clear that granting jurisdiction to the courts of the relevant state (where the land is; where the company has its seat; where the patent is registered etc) will result in the sound administration of justice. In the context of Article 22.2, this will not be the case unless, overall, the proceedings are so closely connected with matters of local company law and internal corporate decision making in respect of the company that the proceedings should not be tried anywhere but in the courts of the state where the company has its seat.*

1 We were told by Mr Tim Lord QC, for BVG, that JPM now asserted that BVG’s liability on the credit protection had risen to US\$157 million.

2 Grupo Torras SA v Sheikh Fahad Mohammed Al-Sabah and others ([1995] 1 Lloyd’s Rep 374.

90 Therefore, I conclude that Teare J reached the right conclusion on the interpretation of Article 22.2, as stated at [46] of his judgment. Put in the context of this case, I agree with him that the question is whether the English proceedings are, "...in substance principally concerned with the ultra vires issue raised by BVG by way of defence to JPM's claim."

### Application of facts to correct interpretation of Article 22(2)

Counsel for Berliner (Mr Lord) then attacked the trial judge's analysis and conclusions following the application of the overall judgement approach. In dealing with this line of argument, Lord Justice Aikens said:

"96 Mr Lord attacked Teare J's analysis and conclusions using the "overall judgment" approach. He submits that the judge failed to take a step back and put the ultra vires issue in its proper context. Mr Lord emphasises, first, that the ultra vires point is potentially dispositive. Secondly, he notes that, logically, the ultra vires [point] is the first point to arise for decision, because if the decision of the BVG boards to enter the JPM [Swap] was ultra vires. then the claim for a declaration as to its validity and the monetary claim under the JPM Swap must fail. In this regard, Mr Lord points out that the judge himself characterised the issue of ultra vires as "...an important preliminary issue." Thirdly, Mr Lord submits that the ultra vires issue is central to JPM's first claim for a declaration as to the validity of the JPM Swap. Lastly, Mr Lord argues that the German law issue on ultra vires is both significant and very substantial and so would be likely to occupy a considerable part of any trial.

99 The judge identified the following issues as being likely to arise in any trial of the disputes between

JPM and BVG in relation to the JPM Swap. (1) How the JPM Swap works according to its terms. This issue has to be considered in order to deal with the allegation of BVG that JPM gave incorrect advice about the nature and working of the JPM Swap and that JPM made misrepresentations about it, failed to disclose relevant matters and otherwise was in breach of contract. (2) What was said and understood (or not) at the meetings between JPM and BVG between June 2006 and July 2007 regarding the JPM Swap and how it worked. Those events have to be analysed to deal with BVG's allegations of the incorrect advice, misrepresentation, non disclosure and breach of contract, which BVG says were the result of what JPM (or those for whom it is responsible) said or wrote at or between meetings in that period. (3) The ultra vires issue. This will involve looking at the relevant German law and also the constitution of BVG. As the judge noted, this issue arises independently of the first two I have summarised.

100 The judge accepted that the ultra vires issue is important because it might be dispositive of the proceedings. He gave weight to that point. But, like the judge, I find it difficult to characterise these proceedings as being "principally concerned with" the ultra vires issue. At this very early stage of the proceedings and on the very limited material we have, I find it hard to see how the ultra vires issue could be completely isolated from the others. The issue (and therefore the German law evidence) will surely have to be placed in the context of the narrative of the meetings and negotiations and a detailed analysis of the nature of the JPM Swap itself to see if resolutions to conclude that contract were ultra vires the powers of the two boards of BVG.

101 Therefore, like the judge, I would characterise these proceedings as being "principally concerned with" the validity of the JPM Swap and whether JPM can enforce its rights under it. As a part of that overall issue, the court will have to consider various defences put forward by BVG, of which an important one, which could be decisive, is the ultra vires issue. But, the ultra vires issue is not the focus of the proceedings as a whole.

102 The judge also looked at this question from the viewpoint of whether the proceedings were so likely to be connected with the German law of ultra vires that they should not, as a matter of the sound administration of justice, be tried anywhere but the courts of Germany. I have already summarised the points that the judge took account of under this heading.<sup>3</sup>

106 Accordingly, I agree with the judge that the ultra vires issue, viewed in its context, is not one which the policies underlying Article 22 generally or Article 22.2 in particular require a decision by the German courts."

The German court has also referred a series of preliminary questions to the European Court of Justice (the "ECJ"). The Court of Appeal considered that it was not appropriate to stay the English proceedings to await the outcome of the ECJ's preliminary ruling. Accordingly, a stay of the English proceedings was refused.

The Court of Appeal decision represents good news for financial institutions. This decision, together with the recent decision in *Depfa Bank & anor v Provincia di Pisa* [2010] EWHC 1148, show that a counterparty in a Regulation country will not easily be able to defeat the jurisdiction of the chosen contractual jurisdiction (in Europe, typically the English courts) by its home jurisdiction simply by alleging that its decision to enter into the swap transaction was invalid.

3 [26] above.

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## Council Regulation (EC) No 44/2001

### Article 22

The following courts shall have exclusive jurisdiction, regardless of domicile:

1. in proceedings which have as their object rights in rem in immovable property or tenancies of immovable property, the courts of the Member State in which the property is situated.

However, in proceedings which have as their object tenancies of immovable property concluded for temporary private use for a maximum period of six consecutive months, the courts of the Member State in which the Defendant is domiciled shall also have jurisdiction, provided that the tenant is a natural person and that the landlord and the tenant are domiciled in the same Member State;

2. in proceedings which have as their object the validity of the constitution, the nullity or the dissolution of companies or other legal persons or associations of natural or legal persons, or of the validity of the decisions of their organs, the courts of the Member State in which the company, legal person or association has its seat. In order to determine that seat, the court shall apply its rules of private international law;
3. in proceedings which have as their object the validity of entries in public registers, the courts of the Member State in which the register is kept;
4. in proceedings concerned with the registration or validity of patents, trade marks, designs, or other similar rights required to be deposited or registered, the courts of the Member State in which the deposit or registration has been applied for, has taken place or is under the terms of a Community instrument or an international convention deemed to have taken place.

Without prejudice to the jurisdiction of the European Patent Office under the Convention on the Grant of European Patents, signed at Munich on 5 October 1973, the courts of each Member State shall have exclusive jurisdiction, regardless of domicile, in proceedings concerned with the registration or validity of any European patent granted for that State;

5. in proceedings concerned with the enforcement of judgments, the courts of the Member State in which the judgment has been or is to be enforced.

### Article 25

Where a court of a Member State is seised of a claim which is principally concerned with a matter over which the courts of another Member State have exclusive jurisdiction by virtue of Article 22, it shall declare of its own motion that it has no jurisdiction.