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IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS
OF ENGLAND AND WALES
KING'S BENCH DIVISION
COMMERCIAL COURT



Case No: CL-2022-000384

Rolls Building
Fetter Lane
London, EC4A 1NL

NCN: [2023] EWHC 1758 (Comm)

Friday, 16 June 2023

Before:

MR JUSTICE FOXTON

B E T W E E N :

SAUDI ARABIAN AIRLINES CORPORATION

Claimant

-and-

SPRITE AVIATION NO. 6 DESIGNATED ACTIVITY COMPANY

Defendant

MR S THOMPSON KC and MR T STEWART COATS (instructed by Norton Rose Fulbright)
appeared on behalf of the Claimant.

MR E. CUMMING KC and MS C HARTSTON (instructed by Pillsbury Winthrop Shaw Pittman
LLP) appeared on behalf of the Defendant.

J U D G M E N T

(via Microsoft Team)

MR JUSTICE FOXTON:

- 1 This is an application by the defendant, Sprite Aviation No.6 (“Sprite”), for summary judgment against the claimant, Saudi Arabian Airline (“Saudia”) for sums allegedly due in connection with the operating lease of an aircraft, pursuant to which Saudia was the lessee and Sprite the lessor. Judgment is sought in respect of two amounts: first, a claim for outstanding rent of \$2,758,732.40 (alleged to be rent rather than supplemental rent), and said to be due under clause 12.2(c) of the Common Terms Agreement (“CTA”); and, second, a debt of \$200,000, which it was agreed would be paid by Saudia in lieu of performance of the obligation it would otherwise have had to redeliver the aircraft in compliance with certain delivery conditions.
- 2 The matter first came before me last week, on 9 June, at which stage Sprite was seeking judgment on admissions in respect of these amounts under CPR r.14.3. As I observed on that occasion, it was clear that Saudia did not dispute that Sprite was entitled to credits in those sums, but, whilst its Reply was not ideally expressed, I am satisfied that Saudia was denying Sprite’s entitlement to judgment in those amounts because it asserted a right to set them off against Saudia’s larger claim. Thus, paragraph 4 of the Reply says that the only reason that those sums have not been paid to Sprite is because they fall to be set off against the larger sum due from Saudia to Sprite as claimed in the Particulars of Claim. Paragraph 6 of the Reply then expressed the mathematical effect of such a netting off.
- 3 I am also satisfied that, coming into that hearing, Sprite understood Saudia’s answer to its claim to be one of set off, because its skeleton argument made extensive submissions as to why no defence of set off was available. Saudia, for its part, advanced argument in its skeleton as to why there was an entitlement to set off. In the face of the clear understanding of both parties, I am not persuaded that any alleged deficiencies in the pleading (which it has not been necessary for me to explore) provided a realistic basis for Sprite seeking judgment on admissions.
- 4 In its skeleton argument for that hearing, it would appear that Sprite had come to the same view because the principal emphasis of its application for judgment was by reference to the absence of a legal right to set off, either because that right was excluded by contract or because it was not available in law. That point having been raised, I identified two authorities which I thought could be relevant to the legal argument to come and notified the parties the day before that I would welcome submissions on them.
- 5 At the hearing, Mr Thompson KC for Saudia took the procedural objection that no claim for summary judgment had been issued and he suggested that he or his client would be in a position of difficulty in responding at that hearing to such an application or, indeed, any application other than one seeking judgment on an admission. It is fair to say that I was somewhat sceptical of that assertion, but given Sprite’s failure to seek summary judgment and the fact that certain authorities had been identified at a late stage by the court, I adjourned the hearing for seven days and required Sprite to issue an application for summary judgment. That has now been done.
- 6 The principal question debated at this hearing was whether rights of set off were excluded by the aircraft lease and, if so, whether that exclusion extended to all rights of set off or only some. Sprite relies on clause 5.12 of the CTA, a clause of a kind commonly found in aircraft leases and usually described as a “net lease clause”. This provides:

“The Lease is a net lease. Lessee’s obligation to pay Rent and to perform all of its other obligations is absolute and unconditional. Lessee shall not regard its obligations as ended, suspended or altered in any way because of any defence, set-off, counterclaim, recoupment or other right of any kind or of any other circumstance”.

Sprite also points to the fact that clause 5.20 confers an express right of set off in relation to debts due between the parties on Sprite but not on Saudia.

7 What does Saudia say now? There is extensive complaint in its skeleton to the fact that Sprite has been extremely slow in taking the point, and that clause 5.12 has not been pleaded by Sprite. It is fair to say that an argument by reference to a no set-off clause has emerged rather later in the history of aircraft lease litigation concerned with outstanding rent than the court is accustomed to see. However, no legal reason has been identified as to why the delay in taking the point should preclude Sprite from relying on it, nor was there a realistic suggestion that Saudia could not deal with the argument at this hearing. To the extent that the point is taken that the clause is not pleaded, I am not satisfied that that is a reason for me not to take it into account in considering whether there is an arguable defence to the claim, but, in any event, if necessary I grant permission to serve the late Reply to Defence to Counterclaim provided last night which squarely raises the clause.

8 Turning to the merits, Saudia contends that the third sentence of clause 5.12 only prevents Saudia *regarding* its obligation to pay as being ended, suspended or altered in any way because of any defence, set off, etc., and that the language is not strong enough to prevent such a defence arising in fact. With respect to Mr Thompson, that is an utterly hopeless contention, which only has to be articulated to be rejected. That kind of tortured and strained construction is to be deprecated in the context of what was clearly a carefully drafted commercial contract between two commercial parties, such as the CTA.

9 In *International Lease Finance v. Buzz Stansted Limited* [2004] EWHC 292 (Comm), Aikens J had to consider whether a right of set off had been excluded under an aircraft lease. In that case, two clauses in the lease were relied upon as excluding the right of set off. The first, Article 5(7) was, I accept a particularly clear no set-off clause. It provided:

“No deductions or withholdings or payments by a lessee under this lease, including the rent repayment, rent reserves, default interest, fees, indemnities or any other item, will be paid in full without any deduction or withholding whether into set off, counterclaim, duties or taxes.”

10 The second clause which Aikens J described as “equally important” was Article 5.9(1). This provided:

“Net Lease

This lease is a net lease and lessee’s obligation to pay rent and make other payments in accordance with the lease shall be absolute and unconditional under any and all circumstances and regardless of or events.”

Aitkens J held that, reading those clauses together, the right of set off asserted in that case was excluded. At [29], he noted that the terms of Article 5.7 were very wide and “could not be plainer”, but he then continued:

“... but if that were not enough Article 5.9.1 stipulates that the lease is a net lease and the lessee’s obligation to pay rent and make other payments in accordance with the lease will be ‘absolute and unconditional under any and all circumstances and regardless of other events’. Once, again, in my view, that wording could not be plainer”.

11 The wording of Article 5.12 here includes language which is similar to that considered in Article 5.9 of the lease before Aitkens J, including the language providing that the obligations are absolute and unconditional, but it goes further and provides that the obligation to pay rent and perform all other obligations is not “to be altered in any way because of any defence or set off”. In my view, those words are clearly sufficient to exclude any right of set off against amounts due from Saudia under the lease.

12 That leaves Mr Thompson KC’s contention that it is at least arguable that the clause extends only to equitable set off and not legal set off. However. I am satisfied that the words “any defence” and “any set off” are sufficiently wide to do exactly that. In any event, the argument is, with respect, a surprising one. For there to be an equitable set off, there must not only be a transactional connection between claim and cross-claim, but it must be manifestly unjust to allow one claim to be enforced without taking account of the other. It is a set off of that kind which businesspeople would ordinarily expect to have available to them rather than a species of set off which requires no connection between allegedly liquidated amounts. A decision to exclude the former but not the latter would be a surprising decision to make. It is for that reason that parties generally try to run the reverse argument,, in my experience, invariably unsuccessfully, that a clause only excludes the right of legal set off and not that of equitable set off. Such an argument was considered and rejected by the Court of Appeal in *FG Wilson (Engineering) Limited v. John Holt & Co (Liverpool) Limited* [2013] EWCA Civ. 1232. Longmore L.J at [36] stated:

“That would be a most surprising result. Indeed, the average businessman who was told that a clause of this kind applied to legal sets off but not equitable set offs would hardly be able to contain his disbelief”.

13 To my mind, the converse is equally true. These clauses are included in leases of this kind in a context in which cash flow is important and they are intended to prevent disputed crossclaims reducing the amount received by way of rent. That commercial need is, if anything, truer of legal debt set off arising from unconnected transactions than of equitable set off. Patton LJ agreed with Longmore LJ, and said at [59]:

“The word used in the relevant condition are clear and it must be assumed that the condition was drafted in this way to which its obvious commercial purpose of ensuring the price is paid free of any underlying dispute about the goods sold or any related matter.”

That is, in my view, the obvious and well-known purpose of the net lease clause here.

- 14 Finally, I would note that clause 5.20 expressly provides for a right of legal debt set off by the lessor. That would make the suggestion that clause 5.12 only applied to equitable set off and not legal set off on the part of the lessee even more surprising. In these circumstances, I am satisfied that the construction argument put forward by Saudia is simply unarguable, but, in any event, it is an argument that the court can and should determine now. The notion that factual matrix evidence at trial could inform the meaning of a clause of this kind in a set of standard aircraft lease terms is fanciful.
- 15 That leaves the claim for \$200,000. As I have said, that is payable under a separate agreement concluded when the aircraft was redelivered in lieu of performance of obligations that arose under the lease. Clause 4.3 of the Redelivery Certificate, which recorded that agreement, provides that various clauses of the CTA were incorporated into and applied to payments due under the Certificate. The clauses thereby incorporated were very specifically targeted and a decision was taken, for whatever reason, to exclude three of the terms of the CTA: clauses 5.11, 5.12 and 5.13. Having given express thought to those parts of the CTA which were to apply to the obligations in relation to the \$200,000 under the Redelivery Certificate, it would, to my mind, be very unlikely that the parties intended that Sprite could, nonetheless, rely upon other terms of the CTA not so incorporated.
- 16 Given the need for clear words to exclude a right of set off, which is a general right available to parties as a matter of law (by reference to the principle in *Modern Engineering v. Gilbert Ash* [1974] AC 689), I am not persuaded that there has been any exclusion of the right of set-off in relation to the \$200,000.
- 17 That leaves the question as to whether there is, nonetheless, no right of set off in relation to the \$200,000 because the requirements for an equitable set off are not made out. That contention was addressed in some detail in the skeleton argument served for the last hearing by Sprite, but, if I may say so, very sensibly, not pressed to any great extent at the hearing. The test for an equitable set off is that it would be manifestly unjust to allow one party to enforce its claims without taking the crossclaim into account because the claims are so closely connected. That test is set out in *Geldof Metaalconstructive NV v Simon Carves Ltd* [2011] 1 Lloyd's Reps 517 at [43]. I accept that the fact that the claims arise from the same trading relationship or transaction is not on its own determinative of the existence of the requisite connection (see *Esso Petroleum Co Ltd v Milton* [1997] 1 WLR 938 and 951), but it must be noted that the observation in that case was made in the context of a dispute where there was an overall umbrella agreement between the parties, under the auspices of which individual contracts of sale were entered into from time to time, and in which the defendant had ordered fuel, pursuant to those individual contracts, without intending to pay for it with a view to setting off future losses under the umbrella agreement which had yet to occur, as and when they did. It might equally be noted that the fact that claims arise under two separate contracts is not of itself enough to prevent them being sufficiently closely connected for an equitable set off as the decision in the *Simon Carves* case makes clear.
- 18 In this case, Saudia says that it has spent money maintaining the aircraft for which it is entitled to a contribution from money paid to Sprite and held by way of maintenance reserves. To the extent that Saudi itself became liable to pay further sums in respect of assumed maintenance expenses on Sprite's part, in respect of exactly the same aircraft under the same lease. In each case, the work was done to ensure the effective use of the same chattel. It is clearly closely connected with the claim that Saudia puts forward. It would be manifestly unjust, in my view, for Sprite to demand payment for the work it needed to do while refusing to pay for the work that Saudia had to do.

- 19 To the extent that reliance is placed on the alleged weakness of Saudia's claim, I am not in a position to form any view as to its merits. It is to be, at least in part, the subject of a preliminary issues hearing.
- 20 In his written argument, Mr Cumming pointed to the principle in time charter cases under the rule in *The Nanfri* [1978] 2 Lloyd's Rep 132, which restrict a right of set off against hire to claims which relate to the total or partial interruption of service or which deprive or prejudice the charterer in their use of the ship. The issue of whether the rule in *The Nanfri* applies to payments under an aircraft operating lease is a rather big question. I am not aware of any case which suggests that *The Nanfri* applies in that context. In any event, in this case, the only live claim where this point arises is not for hire, but for a payment due in lieu of redelivering the aircraft in compliance with the redelivery conditions. That is not analogous to the payment of hire under a time charter.
- 21 In any event, I would suggest that great caution is required before applying the rule in *The Nanfri* to other commercial contexts. This seems to me a situation in which there is a genuine distinction between land rats and water rats, as Stewart Boyd KC once put it when describing the relationship between shipping law and the law of contract generally (see [1993] LMCLQ 317) or, perhaps, more accurately, between bats and water rats (taking account of the aircraft lease context). In the *Carves* case at [26], Rix LJ (who had great familiarity with the rule in *The Nanfri* and its context) described the rule as one arrived at against the background of the special freight rule in *The Aries* and observed that the court in *The Nanfri* "fashioned its own solution to that problem which does not concern us here". That observation is scarcely encouraging of attempts to extend *The Nanfri* outside of its maritime domain,
- 22 Finally, in his written argument, perhaps playing to the assumed prejudices of the historically common law court in which this claim is brought, Mr Cumming made various appeals to the dangers of importing equitable doctrines into commercial transactions. Whatever the merits of that argument when looking at the relief against forfeiture, concepts of constructive notice or the creation of equitable interests, it has never extended to the doctrine of equitable set off which common lawyers have long been content to adopt as one of their own.
- 23 That leaves Saudia's application for a stay of execution in relation to the rent claim. Clearly, the mere existence of Saudia's claim is not reason in itself to grant a stay. There are countless judgments of this court which have refused stays on that basis, where the parties have bargained for no set off, either by a clause to that effect or because the particular claim (e.g. for freight) is one which is not legally subject to a defence of set off. The court will not by procedural means deprive one party of the benefit of the contractual bargain it has obtained.
- 24 It is open to Saudia to seek a stay on other grounds. The grounds it puts forward, as well as its over topping claim, is the fact that Sprite is based out of the jurisdiction and an attempt to suggest that Sprite's financial status is either weak or shadowy. That contention has been significantly answered by a letter from Sprite's solicitors of 13 June. On the basis of that letter, Sprite's accounts are not overdue. It made a profit in 2021. On the evidence, it has four aircraft and a significant amount of money set aside for maintenance reserves. Its place of incorporation is in the Republic of Ireland. I have seen nothing which would justify a departure from the general rule that a successful party is entitled to the fruits of its judgment,

nor do the email exchanges to which Mr Thompson took me earlier in the story have any bearing.

- 25 In those circumstances, the application for summary judgment for the rent is granted, the application for summary judgment for the \$200,000 is refused and the application for a stay of execution is refused.

LATER

- 26 It now falls to me to reach decisions as to costs as a matter of principle in relation to this matter. First of all, there was an application last week, which I granted, for a preliminary issue. Applications for orders of that kind raise legitimate case management concerns. This was a case in which, for reasons that Mr Cumming explained at the time, Sprite did not want to do what it could have done without the benefit of a preliminary issues order and simply seek summary judgment. Preliminary issue orders have sometimes led to litigation heading off in the wrong direction and require careful consideration. In those circumstances, I am persuaded it was appropriate for Saudia to air its concerns about such a procedural course with the court. It is fair to say that it did not adopt a neutral position on the issue or, indeed, a position of armed neutrality, but something rather than more than that, but, nonetheless, I am satisfied that that was an application that properly came before the court for case management considerations and I am going to order that the costs of the application be costs in the preliminary issue.
- 27 In relation to the other matters raised, it seems to me that the case unfortunately was proceeding upon the wrong procedural track when judgment was sought on admissions rather than by way of summary judgment. Whilst, as I have indicated, I am rather sceptical of the suggestion that Saudia was not in a position to deal with the summary judgment on the merits last Friday, the reality is that that issue only arose because it was only in its skeleton argument for that hearing that Sprite shifted its attention from the form of the pleading to the substance of the so-called defence. As I have confirmed in my earlier ruling, I am satisfied that Sprite had at all times known what Saudia was giving as its reason for not paying these amounts its claim.
- 28 That said, we have reached a hearing today at which Sprite has succeeded in recovering £2.7 million, although it is not succeeded in its application for the \$200,000. Between last Friday and today there has been somewhat a flurry of applications with amendments and strike-out applications and so forth. I would observe that, with the great benefit of hindsight, this is a case in which there has been a great deal of thought about procedural matters at the end of this phase of the litigation, and perhaps not quite as much as would have been beneficial at an earlier stage.
- 29 Taking all of those matters into account, I am satisfied that the appropriate order is that Sprite should get all of its costs of the admission application up to the end of last Friday's hearing, but that there will be no order as to either party's costs in the period thereafter.
- 30 It is conceded that, and realistically had to be, that the costs of the action insofar as the rent claim is concerned should be paid by Saudia to Sprite and I so order.

CERTIFICATE

Opus 2 International Limited hereby certifies that the above is an accurate and complete record of the Judgment or part thereof.

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Official Court Reporters and Audio Transcribers
5 New Street Square, London, EC4A 3BF
Tel: 020 7831 5627 Fax: 020 7831 7737
civil@opus2.digital*

This transcript has been approved by the Judge.