



Neutral Citation Number: [2023] EWHC 2874 (Comm)

Case No: CL-2022-000643

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
COMMERCIAL COURT (KBD)

Date: 16/11/2023

Before :

MR JUSTICE FOXTON

Between :

CHOCOLATE CITY LIMITED

Claimant

– and –

WEA INTERNATIONAL INC.

Defendant

Nathan Searle and George Harnett (instructed by Hogan Lovells International LLP) for the Claimant

Tamara Oppenheimer KC and Gillian Hughes (instructed by Dentons UK and Middle East LLP) for the Defendant

Hearing date: 6 November 2023

Draft Judgment Circulated: 9 November 2023

Approved Judgment

I direct that no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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THE HONOURABLE MR JUSTICE FOXTON

This judgment was handed down by the judge remotely by circulation to the parties' representatives by email and release to The National Archives. The date and time for hand-down is deemed to be Thursday 16 November 2023 at 10:30am.

The Honourable Mr Justice Foxton:

INTRODUCTION

1. This is an application by the Claimant (“**Chocolate City**”), a Nigerian music company, for summary judgment under CPR Part 24. Chocolate City seeks declarations to the effect that it is contractually entitled to prepay the amount outstanding under a convertible term loan facility (“**the Facility**”) made to it by the Defendant (“**WEA**”), part of the Warner Music group of companies, ahead of the specified maturity date, and specific performance of certain contractual obligations which would arise if its construction of the Facility is correct. WEA cross-applies for summary judgment for a declaration that Chocolate City is not entitled to prepay the Facility.

The Facility

2. The Facility, which is a detailed and technical document, was entered into between the parties dated 27 March 2019. It is entitled “Facility Agreement in respect of USD1,832,500 Convertible Term Loan Facilities.” The provisions which featured in argument are set out in the following paragraphs.

3. Clause 6.1 provided:

“Repayment of Loans

Subject to clause 7 (Conversion), the Borrower shall repay the Loans in full together with any interest accrued thereon on the Maturity Date.”

(the Maturity Date being defined as “the date falling sixty (60) Months after Financial Close”).

4. Clause 7 provided:

“CONVERSION

7.1 Conversion under Option Agreement

In the event that the Lender exercises the Option in accordance with the Option Agreement, the obligations of the Borrower in respect of repayment of the outstanding Loans and payment of any interest thereon (other than any outstanding default interest) under clauses 6.1 (Repayment of Loans) and 9.2 (Payment of interest) shall be discharged in their entirety on the Conversion Date.

7.2 Conversion in respect of Distribution Agreement

Without prejudice to any rights of the Lender under this Agreement in particular clauses 6 (Repayment) and 8 (Prepayment and Cancellation) and this clause 7, the Lender may (but is not obliged to) at any time on or before the Maturity Date enter into a discussion with the Borrower and ADA in respect of a possible conversion of all or a portion of the outstanding

amount of the Loans at the Maturity Date into an unrecouped balance (i.e. recoupable against future amounts) under the Distribution Agreement and an extension of the term of exclusivity under the Distribution Agreement until such converted amount of the Loans into an unrecouped balance is recouped and paid in full, in each case on terms to be agreed between such parties.

7.3 Reborrowing

The Borrower may not reborrow any amount of the Loans reduced in accordance with this clause 7.”

5. Reflecting the fact that the Facility was a “Convertible Term Loan”, clause 7 recognised that WEA would have the right in certain circumstances:
- i) to convert the outstanding debt into equity in Chocolate City in accordance with the terms of an Option Agreement; and
 - ii) to convert the outstanding amount at the Maturity Date into a balance which could be recovered under the terms of an agreement providing for the distribution of Chocolate City’s material (“**the ADA Distribution Agreement**”).

I address those agreements below.

6. Clause 8, which formed the centrepiece of the argument, provides as follows:

“PREPAYMENT AND CANCELLATION

8.1 Illegality

If, in any applicable jurisdiction, it becomes unlawful for the Lender to perform any of its obligations as contemplated by this Agreement or to fund or maintain its participation in any Loan or it will cause illegality to any Affiliate of the Lender for the Lender to do so:

- (a) the Lender shall promptly notify the Borrower upon becoming aware of that event;
- (b) upon the Lender identifying the Borrower, each Available Commitment will be immediately cancelled; and
- (c) the Borrower shall repay the Loans (i) in their entirety immediately upon the Lender notifying the Borrower or such other date as may be specified by the Lender in the notice delivered to the Borrower or (ii) in such manner and at such time(s) as may be agreed between the Parties in writing.

8.2 Financial Close Long Stop Date

In the event that Financial Close [defined as ‘the date on which the Lender gives the Borrower the notification under clause 4.1’] does not occur on or before the Financial Close Long Stop Date, each Commitment shall be cancelled in its entirety.

8.3 Restrictions

- a) Any notice of cancellation or prepayment given by any Party under this clause 8 shall be irrevocable and, unless a contrary indication appears in this Agreement, shall specify the date or dates upon which the relevant cancellation or prepayment is to be made and the amount of that cancellation or prepayment.
- b) Any prepayment under this Agreement shall be made together with accrued interest on the amount prepaid and, subject to any Break Costs, without premium or penalty.
- c) The Borrower may not reborrow any part of a Facility which is prepaid.
- d) The Borrower shall not repay or prepay all or any part of the Loans or cancel all or any part of the Commitment except at the times and in the manner expressly provided for in this Agreement.
- e) No amount of the Commitments cancelled under this Agreement may be subsequently reinstated.
- f) If all or part of a Loan is repaid or prepaid, an amount of the Commitment (equal to the amount which is repaid or prepaid) in respect of the relevant Facility will be deemed to be cancelled on the date of repayment or prepayment.”

7. “Break Costs” are defined as:

“the amount (if any) by which:

- (a) the interest which the Lender should have received for the period from the date of receipt of all or any part of its participation in a Loan to the Maturity Date in respect of that Loan, had the principal amount received been paid on the Maturity Date;

exceeds:

- (b) the amount which the Lender would be able to obtain by placing an amount equal to the principal amount received by it on deposit with a leading bank for a period starting on the Business Day following receipt or recovery and ending on the Maturity Date.”

8. Clause 9.2 provided:

“Payment of interest

The Borrower shall pay all accrued interest on the Loans on the Maturity Date.”

9. Clause 9.4 provided:

“Break Costs

The Borrower shall, within three Business Days of demand by the Lender, pay to the Lender its Break Costs attributable to all or any part of a Loan being paid by the Borrower on a day prior to the Maturity Date.”

10. Clause 12.2 provided for “other indemnities” obliging Chocolate City to indemnify WEA against loss in certain circumstances. These included:

“(a) The Borrower shall, within 10 Business Days of demand, indemnify the Lender against any cost, loss or liability incurred by the Lender as a result of:

(iv) a Loan (or part of a Loan) not being prepaid in accordance with a notice of prepayment given by the Borrower.”

11. Finally, clause 17.21 gave WEA a right to accelerate “all or part of the Loans” following the occurrence of one of a number of identified Events of Default.

The other transaction documents

12. I have already referred to the Option Agreement and the ADA Distribution Agreement, both of which are referred to in the Facility, were concluded on or around the same date, and which I am satisfied formed part of a single transaction with the Facility Agreement and certain other agreements.

The Option Agreement

13. The Option Agreement was entered into by the parties to the Facility and the initial shareholders in Chocolate City. It is governed by the law of the Federal Republic of Nigeria. Its recitals referred to the credit facilities granted by the Facility and the agreement that WEA “shall have the option to convert any and/or all outstanding amounts under the [Facility] into equity in [Chocolate City]”:

- i) Clause 3.1.1 granted “the Option”, defined as WEA’s “irrevocable discretion to convert Outstanding Obligations to Shares in the authorised capital of the Borrower, as granted in terms of clause 27” (a reference which is clearly a mistake – the Option Agreement contains 16 clauses). “Outstanding Obligations” were defined as all sums due and outstanding to the Lender under the Facility Agreement which remain unpaid by the Borrower as at the Option Exercise Date.
- ii) Clause 3.1.2 provided that WEA’s “ability to exercise the Option shall be unfettered and not be subject to any conflicting rights whatsoever (including any existing rights of pre-emption).”

- iii) Clause 3.3 provided that WEA could “notify [Chocolate City] at any time from the date that is six (6) months prior to the Maturity Date of its consideration of the potential exercise of the Option”, and, following service of such notification, WEA became entitled to information “for the purpose of making its consideration as to the exercise of the Option”.
- iv) Clause 3.5 provided that, following service of an Option Notice, Chocolate City was to issue shares to WEA “on the Maturity Date”.
- v) Clause 4.5 provided that, on the exercise of the Option and issuance of the shares, the obligations under the Facility were extinguished, and various security documents were to be released.

The ADA Distribution Agreement

14. The ADA Distribution Agreement was entered into between Chocolate City and a company called Alternative Distribution Alliance, an affiliate of WEA. It is governed by the laws of the State of New York. The recitals to the ADA Distribution Agreement referred to the Facility Agreement. Further:
- i) In clause 1, the term of the ADA Distribution Agreement was stated to be “co-terminous with the Facility Agreement (i.e. the Term shall continue until the earlier of the Maturity Date ... and any termination of the Facility Agreement pursuant to and in accordance with paragraph 17.21 of the Facility Agreement)”.
 - ii) Clause 1 went on to provide that if, on the Maturity Date or “if earlier, the date of termination of the Facility Agreement” (which was clearly a reference to termination under clause 17.21 as referred to in the preceding sentence), there was a net deficit in Chocolate City’s account, the term of the ADA Distribution Agreement would be extended until Chocolate City’s account was “fully recouped.”
 - iii) Clause 1 gave Chocolate City “the right to repay to ADA one hundred percent (100%) of the amount of Company’s unrecouped balance at any time *after* the Maturity Date (or if earlier, the date of termination of the Facility Agreement)” (emphasis added), but no right to pay off the balance before those dates.

Events following the conclusion of the various transaction documents

15. Chocolate City drew down on the Facility in the sum of USD 1,700,000.
16. On 8 September 2022, Chocolate City served a notice (“**the Prepayment Notice**”) on WEA by which it asserted a right to prepay the full amount of the loan together with accrued interest on or before 20 December 2022. The Prepayment Notice was stated to be given under Clauses 8.3(a) and (b) of the Facility Agreement, asserted Chocolate City’s right to prepay the loan, and requested that WEA provide its bank details for prepayment to be made.

17. On 13 September 2022, WEA responded that Chocolate City was not entitled to make a prepayment. WEA did not provide its bank details.

THE APPLICABLE LEGAL PRINCIPLES

18. The parties were in broad agreement as to the principles to be applied in interpreting the Facility Agreement, both sides being content for the court to apply the summary of the principles set out by Lord Hodge in *Wood v Capita Insurance Services Ltd* [2017] AC 1173, [10]-[14].
19. The debate between the parties as to the admissibility of pre-contractual negotiations and their relevance to the interpretative exercise mainly concerned the application of the legal principles to the facts rather than the identification of the applicable principles. It was common ground that the position remains as stated by Lord Wilberforce in *Prenn v Simmonds* [1971] 1 WLR 1381, 1384-85, namely that such “evidence should be restricted to evidence of the factual background known to the parties at or before the date of the contract, including evidence of the ‘genesis’ and objectively the ‘aim’ of the transaction”.
20. Reference was also made to Leggatt LJ’s judgment in *Merthyr (South Wales) Limited v Merthyr Tydfill County BC* [2019] EWCA Civ 526, [39] for the proposition that arguments from surplusage or redundancy “cannot justify the attribution of a meaning that the contract, interpreted as a whole, cannot bear”.

DOES CHOCOLATE CITY HAVE A RIGHT TO PREPAY THE FACILITY BEFORE THE MATURITY DATE?

The language of Clause 8.3(a)

21. There are difficulties with the language of the Facility on both parties’ constructions.
22. So far as Chocolate City is concerned:
- i) Clauses 6.1 and 9.2 clearly provide for payment of principal and interest on the Maturity Date.
 - ii) Chocolate City argues that those provisions are qualified by a right under clause 8.3. That clause appears under the rather unpromising heading “Restrictions”, although the Facility provides that “headings are for ease of reference only”. More substantively, clause 8.3(a) pre-supposes the existence of a right to cancel or prepay which appears elsewhere (“any notice of cancellation or prepayment given by any Party under this clause 8 shall be irrevocable”) rather than purporting to create one. It is accepted that this is the effect of clause 8.3(a) so far as cancellation is concerned (clauses 8.1(v) and 17.2.1(a) being the source of the right to cancel). While it might be said that clause 8.3(a) can both create the right to prepay “under this clause” and regulate the exercise of that right, that “meta-drafting” would be incongruous, and would give clause 8.3(a) a very different function so far as notices of cancellation and termination are concerned, even though the two are treated in the same manner.

iii) A similar problem arises with clause 8.3(d), which contains a prohibition on prepayment or cancellation “except at the times and in the manner expressly provided for in this Agreement”. Whereas there are contractual provisions providing for when cancellation can be notified, Chocolate City are reduced to stating that, so far as prepayments are concerned, clause 8.3(d) simply requires it to repay in accordance with the date it has specified in its clause 8.3(a) notice, turning what is clearly intended to be a limitation on Chocolate City’s rights into a self-certification scheme.

23. For its part, WEA faces the difficulty that, on its interpretation, clause 12.2(a)(iv) of the Facility (with its reference to notice of prepayment given by Chocolate City) is redundant. Chocolate City argued that clause 8.3 would also be redundant. While the words “by any party” in clause 8.3(a) could not apply so far as Chocolate City is concerned, clause 8.3(a) would still have effect in relation to a demand for early repayment made by WEA under clause 8.1(c), as would clauses 8.3(b) and (f). The weight to be accorded to the redundancy inherent in WEA’s construction is limited. As Leggatt LJ stated in *Merthyr*, [39], it is:

“by no means uncommon, including in professionally drafted contracts, to find provisions which are unnecessary and could, without disadvantage to either party, have been omitted.”

24. Ms Oppenheimer KC for WEA sought to bolster her argument on the irrelevance of any surplusage by suggesting that the Facility was an amended version of a Loan Market Association (“LMA”) standard form, from which an express right of prepayment on the borrower’s part was deleted, but the ancillary terms which would have regulated the exercise of that right were left unamended. While there is a glancing reference to the LMA in the definition of confidentiality undertakings, there is nothing in the terms of the Facility itself or the factual matrix objectively known to both parties which makes it appropriate to construe the Facility in the interpretative framework appropriate for amendments to and deletions from a market standard form. This case is far removed from the position contemplated by Diplock J in *Louis Dreyfus & Cie v Parnaso Cia Naviera SA* [1959] 1 QB 498, 513 of “a standard form of words familiar to commercial men and contained in a printed form in general use”. Rightly, reliance on the LMA standard form was not pressed in argument.

25. Considering the language of the Facility in isolation, I am satisfied that WEA has the better of the argument. However, the Facility was not entered into in isolation, but as part of a suite of agreements which included the Option Agreement and the ADA Distribution Agreement. There was no dispute that those agreements formed part of the admissible corpus of materials when determining whether Chocolate City had a right of prepayment under the Facility (Sir Kim Lewison, *The Interpretation of Contracts* 6th, [3.06]). When the focal length of the interpretative lens is shortened to bring these documents into view, the force of WEA’s construction is considerably strengthened:

i) The Option Agreement is described as granting WEA an “irrevocable discretion” to convert the amount outstanding as of the Option Exercise Date into equity, which right is “unfettered and not be subject to any conflicting rights whatsoever.”

Clauses 3.3.1 and 3.5 proceed on the basis that the right of conversion is to be exercised on the Maturity Date, with the ability to obtain information for the purpose of exercising the option becoming available 6 months before the Maturity Date. However, on Chocolate City's construction of the Facility, WEA's "irrevocable" and "unfettered" right can be extinguished before the Maturity Date by Chocolate City affecting prepayment, including in the period after notice of potential exercise of the option has been served.

- ii) While Chocolate City can argue that it was inherent in the Option being defined by reference to "Outstanding Obligations" that it was subject to being extinguished through prepayment, the timing of exercise of the Option provided for in the Option Agreement, and the protected status of the Option, cohere better with WEA's construction. This is not simply as a matter of language but also from the perspective of business common sense. The scheme of the Option Agreement is that WEA is entitled to the information to decide whether its economic interests are better served by obtaining repayment of the debt, or acquiring an equity stake. The economic interests of Chocolate City and its shareholders are to the opposite effect. Giving Chocolate City the ability to defeat the option when the economic calculus would favour its exercise by making prepayment would substantially undermine the value of the Option.
 - iii) The ADA Distribution Agreement does not contemplate prepayment of the Facility Agreement before the Maturity Date save where it is terminated under clause 17.21. While it can fairly be said that this does not contemplate cancellation for illegality under clause 8.1, the fact that the interpretative exercise must swallow a gnat of drafting infelicity does not justify an interpretation which must accommodate a camel.
 - iv) There is no right to pay off any negative balance under the ADA Distribution Agreement before the Maturity Date or termination of the Facility (implicitly under clause 17.21). That is consistent with a transaction structure which embeds WEA's rights recognised in clause 7 of the Facility up to and including the Maturity Date, and presupposes that the Facility will only be terminated on the Maturity Date or pursuant to early termination under clause 17.21.
26. Chocolate City argued that there can have been no intention to give WEA an embedded right to convert debt into equity on the Maturity Date, because the Facility did not impose an obligation on Chocolate City to drawdown the full amount of the Facility, nor did Chocolate City do so. Mr Searle is right to point to this drafting curiosity of the transaction documents, and the scope for argument as to the amount of equity for which outstanding debt can be converted on the Maturity Date if something less than the full amount available under the Facility is drawn down.
27. Neither party invited me to determine that question on this application. It is a difficulty which arises on both parties' interpretations in a scenario where Chocolate City does not prepay, and to an even greater extent if, as Chocolate City contends, it has an unrestricted right of repayment such that the amount outstanding on the Maturity Date need not be the entire amount borrowed.

Commercial purpose

28. It has been observed that interpretation is a unitary exercise “by which each suggested interpretation is checked against the provisions of the contract and its commercial consequences are investigated” (*The Ocean Neptune* [2018] EWHC 163 (Comm), [2018] 1 Lloyd’s Rep 654, [8]). I am satisfied that the commercial purpose of the transaction of which the Facility forms part emerges clearly from the three documents I have identified: WEA acquired a convertible loan, which (subject to illegality or its own decision to terminate the Facility early) gave WEA an embedded right to swap the outstanding debt for equity at the Maturity Date if it decided it was in its economic interests to do so. That commercial purpose lends strong support to WEA’s construction, but Chocolate City’s construction would be inimical to it.
29. WEA also relied on several pre-contractual documents in support of its argument as to commercial position, including a non-binding Letter of Interest (“LOI”) dated 15 August 2018 signed by Chocolate City and Warner Music Inc. (“WMG”) (of which WEA is part), a non-binding Term Sheet dated 17 January 2019 signed by Chocolate City and WEA and certain correspondence.
30. I have reached my conclusion that WEA’s interpretation is to be preferred without the need to have regard to these materials. However, I am satisfied that these documents can permissibly be used to ascertain the commercial purpose of the Facility Agreement (although not to interpret its terms), and that the materials confirm (but do not add to) the commercial purpose of the transaction as it appears from the suite of the transaction documents:
- i) The LOI states that the proposal was for “WMG or its affiliate(s) to provide financing” to Chocolate City “in the form of a convertible note for an aggregate amount of \$1,500,000 ... which ... shall be payable in full or convertible into 60% of the equity interests” of Chocolate City.
 - ii) In an email dated 27 September 2018, WMG explained the “convertible loan structure [the parties] have been discussing” as “the investor (WMG) loans money and at the end of the loan term (after 5 years), the investor (WMG) has the option of accepting a return in the form of (i) principal plus interest or (ii) equity in the company”, to which Chocolate City responded “We are aligned”, and “We are happy to move ahead with the deal”.
 - iii) The Term Sheet states under “Proposed Transaction”, for example, that this was an investment “by way of secured loan, convertible into equity in the Company at the Lender’s option at the Maturity Date”. “Loan Repayment” provides that “If WMG elects not to exercise the Option to convert the Loan into equity ... at WMG’s sole determination and option, all or a portion of the Loan ... may be converted into an unrecouped balance under the Distribution Agreement”.

Rectification for mistake

31. Finally, both parties suggested in argument that the court could rectify the contract for mistake through the interpretative process under the test in *Chartbrook Ltd v Persimmon*

Homes Ltd [2009] UKHL 38; [2009] 1 AC 1101, though their proposed corrections were naturally very different. This point does not arise, and I will say no more about it.

CONCLUSION

32. For these reasons, and notwithstanding Mr Searle's impressive submissions, Chocolate City does not have a real prospect of establishing a right to prepay the loan made to it by WEA, and WEA's construction is correct. Chocolate City fails on its application for summary judgment and WEA succeeds on its cross-application for summary judgment.