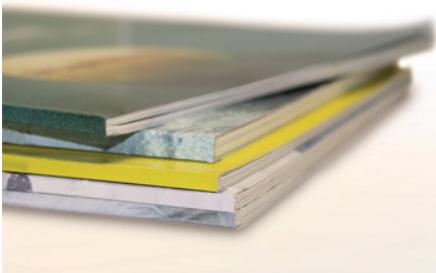


## A Lender's Duties Defined



BY JEREMY HEYWOOD

The recent case of **Mirpuri v. Bank of India** [2010] JRC 129 is one of the very few cases to come before Jersey's Royal Court which touches on the **Security Interests (Jersey) Law 1983** ("the 1983 Law"). The court considered the requirements for a variation of a contract, the nature of a bank's duty to its customers and whether there is a duty on a creditor in an action for debt to mitigate his loss.

The Bank of India ("the Bank") made three loans to Mr. Mirpuri ("the Borrower"), between 2000 and 2003, totaling some US\$ 3.5 million. The Borrower provided security for these loans by the creation of a security interest over a deposit account which he held with the Bank. The deposit account was a multi-currency account which had the option of being designated in either sterling or US dollars. The Bank took control of the deposit account pursuant to Article 2(5) of the 1983 Law. Security interest agreements were entered into in respect of the loans, a term of which was that the Borrower should maintain a margin of 4% in the deposit account over and above the value of the loans.

In September 2005 the deposit account was in sterling. The level of the margin fell below the required 4%. Without reference to the Borrower, the Bank converted some £2 million in the sterling deposit account into US\$ at a rate of 1.7575. The result was that the funds in the deposit account were sufficient to cover the loans, but were below the level of the required margin. In August 2008 the Borrower converted the entire balance of the deposit account from US\$ back into sterling. Sterling promptly entered a period of steep decline against the US\$.

Between November 2008 and January 2009 the Bank wrote to the Borrower on several occasions, informing him that the funds in the deposit account were below the required level, and indeed, did not even cover the loans. Ultimately the Bank notified the Borrower that there had been an event of default and made a formal demand that such be remedied. In March 2009 the Bank appropriated the deposit account and applied it against the loans. The total outstanding was just under US\$650,000. The Bank

instituted proceedings to recover that sum and was successful in an application for summary judgment.

The Borrower appealed and argued that the security agreements did not confer a power on the Bank to convert the currency of the deposit account in 2005, and the Bank's actions in assuming such a power amounted to a variation of the contract, so as to impose a duty upon the Bank to monitor the exchange rates and undertake currency conversions on behalf of the Borrower after 2005 in order to ensure the funds in the deposit account did not fall below the required level.

The Royal Court dismissed this argument on the basis that the terms of the original security agreements were already wide enough to permit the Bank to make the unilateral decision to convert the currency of the deposit account in 2005. It followed that there could not be a variation of the terms of the contract, as such terms were already in the original contract and there would also be no "cause" even if there were a variation (*cause* is similar, but not identical, to the English concept of consideration). The court further held that, even if the original security agreements did not confer upon the Bank the requisite power, a variation of contract could not arise simply because of the Bank's conduct. The court held that the requirements for a valid variation of a contract are the same as for a valid contract, as set out by the Royal Court in **Selby v. Romeril** [1996] JLR 210; namely capacity, consent, *objet [object]*, and *cause*.

Following on from the requirements for a variation of a contract, the court further rejected the contention that the contract between the Bank and the Borrower had been varied in the context of 'offer and acceptance'. The court considered whether an assumption by the Bank of a power to convert the currency of the deposit account amounted to an 'offer' by the Bank to assume a duty towards the Borrower to monitor the exchange rates and protect the value of the deposit account for the Borrower's benefit. The court rejected this argument as being "not reasonably arguable" and being "quite contrary to the normal relationship between a bank and its borrower". The court referred to **Toothill v. HSBC Bank Plc** [2008] JLR 77 with approval and stated that a bank and its borrower are on opposite sides of a contract and that a bank owes no duty, in tort or in contract, to advise the borrower and is entitled to have regard solely to its own interests. The court suggested that it would require very clear evidence before finding that a plaintiff bank, as lender, had assumed such an obligation towards a defendant borrower.

The Borrower argued in the alternative that the Bank failed to mitigate its loss by not converting the funds in the deposit account from sterling to US\$ sooner than it did. The court stated that this point was unarguable as it was, in effect, a way of trying to imply into the security interest agreement or the loan agreements some form of duty on the bank to monitor and protect the value of the security. The court drew the distinction between claims for payment of a debt and claims for damages, and

noted that the relevance of the distinction is that the rules on damages, such as remoteness and mitigation, do not apply to claims for a debt. The court held that in a simple action for the recovery of a debt (in the absence of contractual or other legal obligation

to the contrary) there can be no duty on the plaintiff to mitigate its loss and the principles of mitigation are simply inapplicable.

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