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Hazards in Trade Finance: Court of Appeal Considers Issues of Assignment, Set-Off and Competing Agreements

Introduction

Navigating the course of trade finance is not without its hazards and challenges. Varying trade arrangements and multiplicity of parties often give rise to legal issues and uncertainties. These issues are particularly relevant at this time, when markets are facing increasing financial distress, and lenders are faced with the enforcement of debentures, pledges or assignments pursuant to trade finance facilities.

In *CIMB Bank Bhd v World Fuel Services (Singapore) Pte Ltd* [2021] SGCA 19, the Singapore Court of Appeal had the opportunity to consider such issues of trade finance, including claims under assignment, the resolution of competing contracts, and the right of set-off.

In this case, the borrower allegedly assigned to the plaintiff bank its rights under certain transactions with the defendant. The bank claimed against the defendant as assignee for the purported debts owing from the defendant to the borrower. However, the defendant disputed the terms which governed the transactions between the defendant and the borrower – in particular, the Court had to grapple with a clause *precluding* the right of set-off contained in the borrower's standard terms and conditions on one hand, and a subsisting offset agreement *providing for* the right of set-off between the defendant and the borrower on the other hand.

The Court of Appeal found that the right of set-off in the offset agreement took precedence over the clause precluding the right of set-off in the standard terms and conditions. The bank's claim against the defendant was thus dismissed as the defendant was found to have set off the entire sum due to the borrower.

This decision highlights the pitfalls that may arise in the course of trade finance arrangements and provides an indication of how the courts will interpret common clauses such as assignments and set-off provisions, particularly in the context of competing agreements. This Update looks at the key points of the Court's judgment and the issues that should be considered by banks and borrowers alike when entering into trade finance agreements.

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Brief Facts

CIMB Bank Berhad ("**CIMB**") had provided a loan facility to Panoil Petroleum Pte Ltd ("**Panoil**"), pursuant to which Panoil had purportedly executed a debenture ("**Debenture**") in favour of CIMB. The Debenture allegedly assigned to CIMB rights under 11 Invoices and Sales Confirmations issued by Panoil ("**Sales Documents**"). The documents related to 11 separate sales of marine fuel oil by Panoil to World Fuel Services (Singapore) Pte Ltd ("**WFS**").

When Panoil encountered financial troubles, CIMB sought to exercise its rights as legal assignee under the Debenture against WFS. CIMB sought payment from WFS for sums due under the Invoices. WFS disputed the authenticity of the Debenture and submitted that it had set off the entire sum due to Panoil under the Invoices.

Notably, CIMB relied on certain provisions in "Panoil's Terms and Conditions For Sales of Marine Fuel" ("**Panoil's Terms and Conditions**") which provided that contracting parties are obliged to pay Panoil for each sales invoice free of set-off ("**Clause 8.2**"). Panoil's Terms and Conditions were purportedly incorporated by reference in each of the 11 Panoil Sales Confirmations to WFS.

Conversely, WFS claimed that the transactions with Panoil were subject to on an offset agreement entered into with Panoil which provided for the mutual setting off of certain payable sums between WFS and Panoil ("**Offset Agreement**").

Holding of the Court of Appeal

Authenticity of Debenture

On the facts, the Court of Appeal found that CIMB had proven the authenticity of the Debenture. Here, CIMB had adduced the original Debenture in evidence. Although CIMB did not call the Panoil officers who had signed the Debenture and/or allegedly witnessed Panoil's common seal being affixed to the Debenture, the Court found that the circumstantial evidence to establish the authenticity of the Debenture was overwhelming.

Right of set-off

The Court considered whether WFS was entitled to rely on the Offset Agreement for a right of set-off, which would depend on (a) whether the Offset Agreement applied to the relevant transactions; and (b) whether it was superseded by Clause 8.2.

On the facts, the Court found that the Offset Agreement would be construed as a master contract which was intended to and did *prima facie* apply to all contractual transactions between WFS and Panoil.

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Further, neither the fact that the 11 Invoices and Sales Confirmations between Panoil and WFS did not refer to the Offset Agreement, nor the fact that neither party had ever exercised any right of set-off for three years thereafter, raised a presumption that the Offset Agreement would not apply to the transactions. The Court thus found that the Offset Agreement was in fact intended to apply to the transactions.

The Court then considered whether the Offset Agreement was superseded by Clause 8.2, ultimately answering the question in the negative. Notably, the Court focused on issues of which clause/contract was the more specific document, and which had been specifically agreed to.

The Court of Appeal took a different position from the High Court Judge, who relied on the case of *Sintalow Hardware Pte Ltd v OSK Engineering Pte Ltd* [2017] 2 SLR 372 ("*Sintalow*") to conclude that Clause 8.2 had superseded the Offset Agreement. The High Court Judge's reasoning is summarised below:

- (a) In *Sintalow*, it was held that the more specific document ought to prevail over a standard form document, and that the specifically agreed clause takes precedence over a clause incorporated by reference to the general terms and conditions. Three specific product agreements were thus found to have superseded a master contract between the parties.
- (b) On this basis, the Judge found that Clause 8.2 superseded any rights of set-off under the Offset Agreement. Panoil's Terms and Conditions (including Clause 8.2), which had been incorporated under each of the 11 Sales Confirmations, was deemed to be the more specific contract and should prevail over the terms in the other less specific contracts (the Offset Agreement).

The Court of Appeal disagreed with the Judge's reasoning and distinguished the case of *Sintalow* as follows:

- (a) In *Sintalow*, the master contract contained only *general* terms and conditions. However, the Offset Agreement in this case covered the single substantive issue of the right of set-off, suggesting that the parties had focused on this issue and intended for the right of set-off to apply to their transactions, whereas Clause 8.2 was part of a pre-printed set of general terms and was merely one provision in a set of terms canvassing multiple issues.
- (b) The three product agreements in *Sintalow* which were found to have superseded the master contract had been signed by both parties. In contrast, in the present case, it was the Offset Agreement in this case which was signed by both parties, whereas Panoil's Terms and Conditions and Sales Confirmations were pre-printed documents unilaterally issued by Panoil.
- (c) As the more specific document which had also been specifically agreed to, the Offset Agreement should thus take precedence over Clause 8.2.

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The Court thus held that WFS' right of set-off under the Offset Agreement took precedence over Clause 8.2. WFS was found to have set off the sums due to Panoil under the 11 Invoices, and CIMB's claim was accordingly dismissed.

Concluding Words

This case highlights some of the pitfalls which banks should guard against when dealing with assigned rights. Here, WFS successfully argued that the relevant transactions were subject to the Offset Agreement (which was not referred to in the transactional documents normally provided to CIMB as financing bank to Panoil) which gave WFS the right of set-off, thus defeating CIMB's claim entirely.

Financing banks may justifiably be concerned with the Court of Appeal's decision in this case as it exposes the banks to the risk of hidden contractual arrangements forming the backdrop to debts assigned to the bank, which may have serious impact on the bank's rights. In this regard, parties may wish to note the following key takeaways from this decision, moving forward:

- (a) **Conduct appropriate due diligence** – Due diligence may uncover arrangements which may affect the rights of the bank against the counterparties.
- (b) **Serving Notice of Assignment** – Sending out a notice at the outset when the relevant debt first accrues may flush out hidden facts that may compromise the assignment. However, banks should keep in mind the commercial practicability of such actions.
- (c) **Incorporation of terms** – If parties wish for terms to be incorporated by reference in a particular transaction (such as the Offset Agreement in this case), they should ensure that such terms are clearly referred to in the transaction documents, and that they are specifically agreed to (whether by signature or otherwise).
- (d) **"No set-off" clauses** – To minimise the risk that hidden set-off arrangements will apply to prejudice the bank's rights as assignee, banks may wish to ensure that transactional documents for assigned debts contain express "no set-off" clauses drafted in appropriately wide terms. Alternatively, written confirmations can be sought from the debtor that no rights of set-off will be asserted.
- (e) **Buy-sell arrangements** – WFS here alleged the existence of concurrent buy-sell arrangements between itself and Panoil, which may also be a hidden pitfall for banks, giving the impression that the borrower has a *bona fide* on-sale already lined up for the cargo being financed and affecting the credit risk profile of the borrower. To mitigate against this, banks may wish to require their customers to provide full information on the end-to-end process and trade cycle in respect of the transaction subject to finance.

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For existing financings, Banks may wish to consider whether they are able to seek further information and/or confirmations (as aforesaid) through the exercise of rights under *inter alia* further assurance clauses forming part of the terms of the relevant facility.

For more information on prudent commodity trade financing practices and lending standards for banks in the commodity trading sector, please see our earlier Update on "Association of Banks in Singapore Launches New Code of Best Practices for Commodity Financing" [here](#).

For further information, please feel free to approach our team below.

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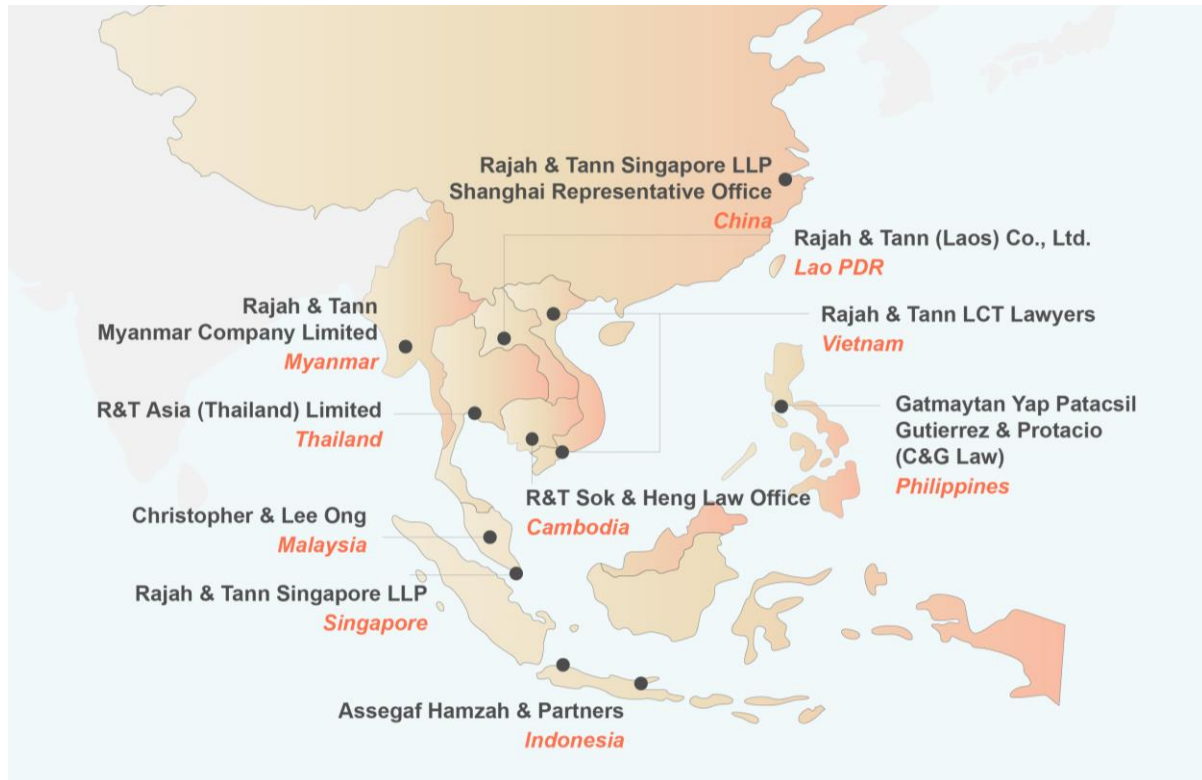
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