



## **Ineffective contracts, restitution and the change of position defence**

About a recent decision rendered by  
the High Court of Justice of London

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ABSTRACT

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The paper, moving from a cross-border case and with a comparative law perspective, addresses which is the operative rule of Restitutionary claim resulting from an ineffective contract, assessing whether it would be achievable, under Italian Law, the same results of the “Change of Position Defence” under common law. The topic relates to the broader issue of allocating costs incurred by the party who performed a void contract in reliance on its validity, for which, under Italian Law, guidance could be given by Section 1328, paragraph 1, second part, of Italian Civil Code.

**Keywords:** Ineffective Contracts; Law of Restitution; Change of Position Defence; Costs borne by defendant in Restitutionary claim.

Il contributo affronta, muovendo da un caso *cross border* e con sguardo comparatistico, la questione del regime applicabile alle restituzioni che conseguono alla declaratoria di nullità contrattuale, focalizzandosi sulla configurabilità, nell’ordinamento domestico, una tutela, per il convenuto in ripetizione, funzionalmente accostabile a quella che il *common law* indica come “*Change of Position Defence*”. Il tema si incentra su quello, più ampio, dell’allocazione dei costi sopportati dalla parte che ha eseguito un contratto nullo confidando nella sua validità, per il quale può guardarsi al principio sotteso all’art. 1328, comma 1°, seconda parte, c.c.

**Parole chiave:** nullità contrattuale; restituzioni; indennizzo del convenuto in ripetizione; *change of position defence*.

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This paper has been subjected to double-blind peer review

## Ineffective Contracts, Restitution and the Change of Position Defence

SOMMARIO: 1. Banca Intesa Sanpaolo spa- Dexia Crediop SA v. Comune di Venezia – 2. The IRS's are void and unenforceable under English Law, according to the High Court, for Venice's officers want of Authority and Venice's lack of capacity to contract under Italian Law – 3. The Applicable Law of the Unjust Enrichment Claim – 4. Law of Restitution *Change of Position Defence* in North American and English Common Law – 5. Restitution under Italian Law and *Change of Position Defence*: some points of potential convergence among the two jurisdictions – 6. The peculiarities of the COPD shaped by the High Court.

### 1. Banca Intesa Sanpaolo spa-Dexia Crediop SA v. Comune di Venezia

A recent decision rendered by the High Court of Justice - Banca Intesa Sanpaolo Spa - Dexia Crediop SA v Comune di Venezia<sup>1</sup> - gives occasion to address the differences and similarity in the Law of Restitution both in common law jurisdictions and, on the civil law side, in Italian law.

Indeed, the peculiarities of the case decided involved simultaneously English and Italian Law.

Intesa and Dexia, the Claimants, are Italian companies carrying on business as banks; the Defendant is the Italian municipal Authority of the world-renowned city of Venice.

The factual background is summarized as follows in the decision (§§ 1 and 2): “1. *In this case: i) The Claimants (the Banks which expression, as the context requires, also extends to the Claimants' predecessors in title) seek declarations that certain interest rate swap (IRS) transactions (the Transactions) which they say they entered into with the Defendant (Venice) on the terms of the 1992 ISDA Master Agreement are valid and binding, and alternative relief in contract and tort if it is found they are not. ii) Venice seeks declarations that the Transactions are not valid and binding (and consequential relief in unjust enrichment), and alternatively relief in contract and tort if it is found that they are. 2. Behind that simple symmetry lurks a complex set of questions raising disputes of pure fact, and of Italian and English law, some of them with potentially profound implications for the sanctity of English law contracts. By way of a very short introduction to those issues: i) Venice contends that, for various reasons, it lacked the substantive power*

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<sup>1</sup> Banca Intesa Sanpaolo Spa – Dexia Crediop SA (Claimants) v. Comune di Venezia (Defendant), before the High Court of Justice Business and Property Courts (England and Wales) King's Bench Division Commercial Court [2022] EWHC 2586 (Comm) Case No: FL-2019-000012 - 14 October 2022.

*to enter into the Transactions as a matter of Italian law, and that, applying English conflict of law principles, that means that it did not have capacity to enter into the Transactions and that they are not valid. ii) The Banks deny that the entry into the Transactions contravened any provisions of Italian law, on the basis of arguments as to the effect of Italian law and its application to the facts of this case, and further deny that any such contravention would deprive Venice of capacity to contract as a matter of English conflict of laws principles in any event. iii) Venice also contends that the Transactions breached various rules of Italian law which have the status of "mandatory rules of law" for the purposes of Article 3(3) of the European Union Convention 80/934/EEC (the Rome Convention) and that as a result the Transactions are void and/or unenforceable. iv) On this basis, Venice claims restitution of the net amounts paid under the Transactions to date. The Banks contend that they have a defence of change of position to these claims, and that Venice's claims are time-barred. v) If the Transactions are valid and binding, Venice alleges that the Banks owed Venice a non-contractual advisory duty to assess the suitability of the Transactions, which was breached, and that Venice has suffered loss as a result. vi) If the Transactions are not valid and binding, the Banks allege that Venice was in breach of various contractual duties or is liable to it in respect of various misrepresentations and/or misstatements, for which they claim damages".*

The operative part of the decision reads: (§463): "*For the reasons I have set out above: i) Venice lacked capacity to enter into the Transactions on the basis of the Speculation and Indebtedness Arguments, with the result that they are void and unenforceable as a matter of English law. ii) Venice's challenges to the Transactions based on the Article 42(2)(i) TUEL Argument and breach of mandatory Italian law fail. iii) The Banks' arguments based on estoppel, breach of contract, misrepresentation or misstatement, Article 1338 of the ICC and the indemnity obligation in the Mandate Agreement fail. iv) Venice is entitled to restitution of the amounts paid to the Banks under the Transactions, but the Banks are in principle entitled to rely on a defence of change of position in respect of payments made under the "back-to-back" Hedging Swaps, subject to the reservations at [424] above. v) Venice's alternative claim for damages for breach of non-contractual obligations fails".*

Among the conclusions, it appears significant that Mr Justice Foxton found the Banks entitled, in principle, to rely on a Change of Position Defence (COPD) in respect of payments made under the "back-to-back" Hedging Swaps: a conclusion which makes it interesting to underline differences and similarity (if any) among the two laws the Court has applied, English and Italian and the two legal tradition, common and civil law, to which they pertain.

## **2. The IRS's are void and unenforceable under English Law, according to the High Court, for Venice's officers want of Authority and Venice's lack of capacity to contract under Italian Law**

The derivative contracts (IRS or the Transactions) were entered into under the Venice Master Agreement which embedded a choice of (English) law

agreement and, therefore, according to the Rome Convention, which applied at the date of the Transactions, both *i*) Issues as to the existence of a contract and the *ii*) Issues as to the consequences of a contract being void are governed by the English law chosen by the Parties.

Notwithstanding, this choice of law, according to the Court, the issues as to Venice's capacity of contracting and actual authority on Venice's officers are to be determined by the Italian Law.

Indeed, it is worth noting that the requirement of legal capacity of contracting is considered both in common law and civil law tradition: it was mentioned not only in the Napoleonic Code (art. 1108 del Code Napoleon<sup>2</sup>) and in art. 1104 of the previous Italian Civil Code (the one enacted in 1865 and in force until 1942), but also in para. 984 of the Civil Code of Lower Canada<sup>3</sup>.

In the wording of the decision: “107. *The Transactions are governed by English law. That does not mean that every legal issue which arises for determination is exclusively a matter of English law. In particular, it is common ground that issues as to the capacity of Venice (as a legal person) to enter into the Transactions are to be determined by reference to Italian law: Credit Suisse International v Stichting Vestia Groep [2014] EWHC 3103 (Comm), [185]. This reflects the fact that, as a legal person, Venice only exists by virtue of, and within the confines imposed by, the municipal legal system which brought it into being. It is also common ground that the actual authority of those who purported to commit Venice to the Transactions is a matter of Italian law*”.

Venice alleged its lack of capacity to enter into the Transactions for failure to comply to art. 42 Testo Unico Enti Locali (TUEL) and art. 119 Italian Constitution.

The High Court took into account that: “128. *Venice contends that three of the arguments which it raises have the effect that it lacked capacity to enter into the Transactions: i) The argument that the Transactions were speculative, and as a local authority Venice lacked capacity to enter into speculative derivatives as a matter of Italian law (the Speculation Argument). ii) The argument that the Transactions constituted indebtedness other than for investment expenditure, and as a local authority Venice was not permitted to have recourse to indebtedness otherwise than for the purpose of investment (the Indebtedness Argument). iii) The argument that the Transactions did not receive the requisite approval from the City Council, and Venice consequently lacked capacity to enter into the Transactions (the Article 42 TUEL Argument)*”.

The assessment of the Italian Law concerning such issues was made by Mr Justice Foxton considering a significant decision of the Italian Supreme Court

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<sup>2</sup> Art. 1108 Code Napoleon reads as follows: «Four requisites are essential for the validity of an agreement: The consent of the party who binds himself; His capacity to contract; A definite object which forms the subject-matter of the undertaking; A lawful cause in the obligation».

<sup>3</sup> Which reads: «There are four requisites to the validity of a contract: Parties legally capable of contracting; their consent legally given; something which forms the object of the contract; a lawful cause or consideration».

(Cassazione), rendered by Joint Divisions on 12 May 2020 n. 8770 (referred to as “the Cattolica decision”)<sup>4</sup> in a dispute, involving derivative contracts entered into by a Bank (Banca Nazionale del Lavoro) and the Municipality of Cattolica (a small city along the Adriatic shore): “289. I have set out my reasons at [260] to [261] above for concluding, on the basis of the Cattolica decision, that the Transactions fell within one of the categories of derivative which the Supreme Court held constituted indebtedness or expenditure for the purposes of both Article 119(6) of the Constitution and Article 42(2)(i) of TUEL (the Supreme Court having addressed these issues compendiously)”.

Making reference to such Italian case law, Mr. Justice Foxton found the IRS contracts forbidden to the Municipality of Venice by the Italian Law and therefore being void under English Law: “i) It follows from my conclusion that the Transactions, as a whole, were speculative that they were not undertaken for the purpose of financing investment expenditure” (§268); “269. The conclusions at [267] and [268] necessarily entail that the Transactions contravened Article 119(6) of the Constitution”; accordingly, the reasoning, at §274, reads: “274. Applying English law, and on the basis of Haugesund, the inevitable consequence of my conclusion that, on the basis of the Speculation and/or Indebtedness Arguments, Venice lacked the substantive power or legal ability to enter into the Transactions, is that they are void”; “358. ...Venice lacked the substantive power to enter into the Transactions as a matter of Italian law, with the result that the Transactions are void as a matter of English law”.

As reported above, the Banks had asked, as an alternative remedy in case the Court found the IRS’s to be not valid and binding, for an award of damages in contract and tort. The subordinate claim was raised under art. 1338 Italian Civil Code (ICC), titled “Knowledge of reasons for invalidity” which states: “A party who knows or should know the existence of a reason for invalidity of the contract and does not give notice to the other party is bound to compensate for the damage suffered by the latter in relying, without fault, on the validity of the contract”<sup>5</sup>.

Characterizing the Cattolica decision as a “Fundamental Restatement” of the Italian Law, the High Court has dismissed “The Banks’ Claim Under Article 1338 of the ICC”) reasoning as follows: “381. The short answer to this claim is neither Venice (nor, for that matter, the Banks) “should have known of the invalidity of the Transactions” before the decision of the Supreme Court in Cattolica or were at fault in not doing so. Once again, that wholly ignores the extent to which Cattolica effected a fundamental restatement of Italian law in the relevant respects”.

Indeed, the same characterization of the Cattolica decision is repeated at §426 ss. of the reasoning, whereas the High Court decided that Venice’s Claim for Restitution is not Time-Barred because (§430) “iv) ... the decision of the Supreme

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<sup>4</sup> The Cattolica decision, at para. 10.8, requires the authorization to the Municipality to enter in IRS- particularly if an upfront is provided, must be given by the Municipal Council: otherwise, the contracts are null and void.

<sup>5</sup> The translation of ICC paragraphs quoted in this paper is the one provided by J.H. MERRYMAN, *The Italian Civil Code*, Oceana, New York, 1969.

*Court in Cattolica represented a fundamental change in the interpretation of the relevant legislative and regulatory provisions...; v)... exercising reasonable diligence, Venice could not have discovered that it had a "worthwhile claim" prior to the Cattolica decision in the Supreme Court".*

### **3. The Applicable Law of the Unjust Enrichment Claim**

Being the Transactions void under English law (as *ultra vires* transactions), it follows the parties can reclaim, as Unjust Enrichment, the performance rendered under the contracts: as recalled in the decision (§394), is "*common ground that money paid by one party under a void contract, such as a payment made under a void swap, is in principle recoverable in unjust enrichment*".

Wondering which law applies to the restitutionary claim, the High Court decided it is the English one on two grounds.

Firstly, "*Under the Rome Convention, which applied at the date of the Transactions: i) Issues as to the existence of a contract are governed by the law which would apply if the contract had been concluded (Article 8(1)), which in this case would be English law by virtue of the choice of law agreement in the Venice Master Agreement. ii) Issues as to the consequences of a contract being void are governed by the same law (Article 10(1)(e))*". (§386.)

Secondly, the same conclusion is attained applying the common law test of the closest and most real connection, for the Court having found that in this case "*the unjust enrichment claim has its closest and most real connection with English law by reason of the choice of law clause in the Venice Master Agreement*" (§390).

### **4. Law of Restitution Change of Position Defence in North American and English Common Law**

The change of position defence became a recognized feature of the American law concerning restitution of mistaken payments in the early years of the twentieth century, if not earlier<sup>6</sup>. It has been most recently restated in the following form in the *Restatement (Third) of Restitution and Unjust Enrichment* (2011) in §65: "*If receipt of a benefit has led a recipient without notice to change position in such manner that an obligation to make restitution of the original benefit would be inequitable to the recipient, the recipient's liability in restitution is to that extent reduced*". In the latter part of the twentieth century, it was adopted by Commonwealth courts as an improvement on the traditional defence of estoppel to mistaken payment claims<sup>7</sup>. Estoppel was available as a defence only if the payer represented to the

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<sup>6</sup> F.C. WOODWARD, *The Law of Quasi Contracts*, Little Brown & Co., Boston, 1913, p. 38-42.

<sup>7</sup> See P.D. MADDAUGH – J.D. MCCAMUS, *The Law of Restitution*, Looseleaf Ed., Toronto, 2021, p. 466. In the reasoning: (§402) "*On this basis, I am satisfied (certainly in the particular circumstances of this case) that a defence of change of position is, in principle, available*

payee that the moneys mistakenly paid were due. No such requirement restricts the availability of COPD. Further, any degree of reliance engaged the estoppel doctrine and constituted a complete defence to the claim. With COPD, however, it was recognized that the defence would only be partial in cases where only a portion of the mistakenly paid money had been depleted.

To engage COPD, however, it is necessary to establish that the payee reasonably believed that the mistakenly paid moneys are now owned by the payee and, further, that the payee made a decision to spend the moneys in an irremediable or irrevocable fashion. An oft-cited illustration is that the mistaken payee might decide to spend the money on an expensive vacation that was only undertaken because of the receipt. By way of contrast, mere expenditure of the money on a pre-existing debt would not give rise to the COPD. If the moneys were spent by the payee on the acquisition of an asset that would not otherwise have been acquired by the payee, the residual value of the asset would be deducted from the defence. The detrimental reliance must be irrevocable.

Another aspect of COPD that is relevant in the present context is its availability in the context of “anticipatory” changes of position. Initially, English courts hesitated over whether the decision to make the expenditure of the mistakenly paid funds could be made before the moneys were received. After some initial hesitation, English law now accepts that where the payee is induced to believe that the moneys will be forthcoming from the payer and then decides, in advance of the actual receipt, to detrimentally commit to spending the moneys in reliance on their anticipated receipt, the COPD is available.<sup>8</sup> This became material in the *Intesa* decision as the commitment to expend moneys received from Venice on the “back-to-back” IRS’s was made before the moneys were actually received from Venice.

The natural home for the COPD defence is in the context of mistaken payments where there is no contractual relationship between the parties that requires the payment. As the *Lipkin, Gorman (a firm) v. Karpnale Ltd.*<sup>9</sup> decision illustrates, however, COPD may also be available in cases where a rogue third party misappropriates funds from the claimant and then transfers them gratuitously to the defendant who, in turn, detrimentally relies on that innocent receipt to detrimentally change position. In *Lipkin, Gorman*, a lawyer misappropriated funds from his law firm and gambled them away at the defendant’s casino. The winnings paid by the defendant to the rogue constituted a COPD which reduced the firm’s claim. In this additional context, then, an innocent recipient of funds who reasonably believes that it is entitled to deal with them as it wishes is entitled to rely on COPD.

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*notwithstanding the fact that Venice’s right to restitution arises from the fact that a condition of those payments (a legally enforceable right to the counter-payments) was not satisfied”.*

<sup>8</sup> *Dextra Bank and Trust Co. Ltd. v. Bank of Jamaica*, [2002] 1 All E.R. (Comm.) 193 (P.C.).

<sup>9</sup> [1991] 2 A.C. 548 (U.K.H.L.)



One would not expect, however, that COPD would be available in the context of benefits transferred under ineffective transactions. A critical difference is that the recipient of benefits transferred under an ineffective transaction expects to provide benefits in return. Thus, if moneys are paid as a down payment or partial payment under a void building contract, the builder cannot resist the purchaser's restitution claim on the basis that the builder has spent the moneys on an otherwise unplanned vacation. Unlike a mistaken payments case, the builder has no reasonable belief that the moneys paid require no provision of value in return.

Nonetheless, there is a recent English decision, relied upon in *Intesa*, in which COPD was applied to benefits conferred under a void transaction. In *School Facility Management Ltd. v. Christ the King College*<sup>10</sup>, the doctrine was applied in the context of arrangements for the building of a school facility for the College which proved to be *ultra vires* the College. The College wished to expand its operation and add a new facility. The College did not have the resources to pay for the building of such a facility. Having approached the builder it preferred for this assignment (BOS), arrangements were entered into for the financing of the construction and a lease of the facility to the College. At the risk of oversimplifying somewhat complex factual circumstances, the ultimate arrangements consisted of two agreements, one between School Facility Management (SFM) and BOS and the other between SFM and the College. Under the first, SFM, which raised the financing for the project, hired BOS to build the facility of which SFM became the eventual owner. Under the second, SFM leased the building on a long-term basis to the College which paid rental fees to SFM which were designed to cover, over the length of the lease, the costs associated with the building of the facility which had been paid to BOS by SFM. In due course, the College discovered that its agreement with SFM was *ultra vires*. Among the numerous claims arising from this scenario, the College sought restitution of the moneys it paid to SFM. The trial judge, Foxton J., in a holding<sup>11</sup> not challenged on appeal, held that a COPD defence was available to SFM on the basis of its (anticipatory) payment of the moneys received to BOS.

When a somewhat similar issue with respect to anticipatory commitment of funds to be received in the back-to-back IRS's entered into by the Banks arose in *Intesa*, Foxton J. relied, in part, on the reasoning in *SFM* to reach the conclusion that the COPD was also available in the *Intesa* context. Having ascertained that the IRS's were void under English law, the decision adds that: "*the Banks are in principle entitled to rely on a defence of change of position in respect of payments made under the*

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<sup>10</sup> [2021] EWCA Civ. 1053, [2021] 2 W.L.R. 6129 (C.A.).

<sup>11</sup> *School Facility Management Ltd. v. Christ the King*, [2020] EWHC 1118 (Comm.); [2020] EWHC 1477 (Comm.).

"back-to-back" Hedging Swaps" ( 463)<sup>12</sup>, because "both the payer and the recipient were acting on the basis of an apparent state of affairs that the condition for Venice's payments (the existence of legally enforceable rights to counter-payments) had been satisfied" (§400); "the nature of the change of position contended for by the Banks was not engaging in expenditure wholly unrelated to the obligations arising under the Transactions (sc. the builder who spends the advance payment on a holiday) but entering into and performing contracts entered into for the purpose of hedging their liabilities under the Transactions" (§401); "it is routine and objectively foreseeable that banks entering into transactions of this type will hedge them" ( 401).

The Court notes (§406) "It is now clear from the decisions of the Privy Council in *Dextra Bank and Trust Co Ltd v Bank of Jamaica* [2002] 1 All ER 193 and the Court of Appeal in *Jones v Commerzbank AG* [2003] EWCA Civ 1663, ([38] and [47]) that the defence of change of position can be established by action taken before, but in anticipation of, the receipt of the amounts of which repayment is sought." And adds: "412. In A Restatement of the English Law of Unjust Enrichment (2012), Lord Burrows distilled the law on change of position into the following summary: "(1) The defendant has a defence to the extent that— (a) the defendant's position has changed as a consequence of, or in anticipatory reliance on, obtaining the benefit, and (b) the change is such that the defendant would be worse off by making restitution than if the defendant had not obtained, or relied in anticipation on obtaining, the benefit".

Therefore, in the words of Mr. Justice Foxton, "413. I can find nothing in that summary which would deny the Banks a change of position case where they had entered into back-to-back transactions by which they assumed (conditional) payment obligations in anticipatory reliance of receiving essentially the same payments from Venice. Indeed, the routine and objectively foreseeable nature of that anticipatory reliance, and its "back-to-back" nature (with the Banks' anticipatory reliance essentially mirroring the anticipated receipts) would seem to make this a paradigm case for the availability of the defence of change of position" (...). "424. (...) there is a principled case for recognizing a defence of change of position to the extent of any swap payments made by the Banks under the Hedging Swaps (...)".

Even if one accepts the validity of applying the COPD in the SFM case, however, we may note an important distinction between SFM and *Intesa*. In SFM, the structure of the two agreements was designed, to the knowledge of all parties and to carry out the wishes of the College, to require SFM to pay in advance the moneys to the builder which all parties expected would be reimbursed to SFM by the College by its rental payments. Pursuant to the arrangements, the moneys had already been committed through SFM's payment of the up-front cost of building the facility to BOS. Perhaps, rather than COPD, one might better explain the result

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<sup>12</sup> In the reasoning: (§402) "On this basis, I am satisfied (certainly in the particular circumstances of this case) that a defence of change of position is, in principle, available notwithstanding the fact that Venice's right to restitution arises from the fact that a condition of those payments (a legally enforceable right to the counter-payments) was not satisfied".

on this point in *SFM* on the basis that none of the parties involved expected that *SFM* would be “enriched” by the receipt of these reimbursement moneys from the College. Similarly, one who intentionally enters into an agreement with an agent who, as intended, passes the money provided to the principal would have no restitution claim against the agent if it proved to be the case that the agent acted without the principal’s authority. The agent has not been enriched.

In *Intesa*, on the other hand, there was no similar understanding or requirement that the Banks would necessarily commit the funds received from Venice to servicing the back-to-back IRS’s the Banks entered into for their own purposes.

Mr. Justice Foxton noted (§413) that it was “foreseeable” that the banks would entered into such arrangements. Further, such arrangements were not “wholly unrelated to the obligations arising under the Transactions”. If the intention in *Intesa*, is to create a new version of COPD that applies whenever a payer under a void contract can reasonably foresee that the payee will spend the money in an irretrievable fashion in a manner not wholly unrelated to performance, this new version of COPD would be potentially available in a broad range of ineffective transactions cases. It must often be foreseeable that moneys paid under a transaction will be used in such fashion by the payee. If such a new defence is to be recognized, it may be that it should be limited to expenditures undertaken by the payee that were *necessary* to the payee’s performance of its obligations under the agreement in question or, perhaps, were *intended by the parties* to be used in this fashion. Arguably, that was not the case in *Intesa*.

The effect of the ruling in *Intesa* is to shift the risk of loss incurred by reason of detrimental reliance on the validity of the agreement from the recipients of the benefits, the Banks, to Venice. This might be considered to be appropriate where Venice, (though behaving innocently), is in some sense responsible for the ineffectiveness of the transaction by virtue of its *ultra vires* conduct. No suggestion is made by Foxton J. that this was considered to be a relevant factor in *Intesa*. It may be, however, that if the *Intesa* ruling is to be applied in other ineffective transactions contexts and to the benefit of the party responsible for the ineffectiveness of the transactions, such considerations may become relevant. Consider, for example, a contract rendered ineffective by the commission of a crime where the criminal wishes to rely on COPD.

##### **5. Restitution under Italian Law and *Change of Position Defence*: some points of potential convergence among the two jurisdictions**

Mr Justice Foxton noted, at §393, that “It is common ground that no change of position defence arises as a matter of Italian law”.

It can be doubted that such a conclusion should be so definitive under Italian law.

In particular, it may be interesting to enquire whether Italian Law would give, in some manner, relief and protection to the reliance considered in the change of position defence.

To answer such a question, we cannot rely on art. 1338 ICC, because it requires one of the parties to the contract to be aware of its invalidity or ineffectiveness. The rule is considered an application of the broader principle stated in the previous art. 1337 ICC, which reads “Negotiations and pre - contractual liability” “The parties, in the conduct of negotiations and the formation of the contract, shall conduct themselves according to good faith”

Indeed, the High Court rejected the Banks' Claim under article 1338 of the ICC because: “... neither Venice (nor, for that matter, the Banks) "should have known of the invalidity of the Transactions" before the decision of the Supreme Court in Cattolica or were at fault in not doing so” (§381).

In our case, therefore, there was no room for liability and damages.

On the contrary, the COPD refers to a legitimate reliance of the payee and provides a relief which is not characterizable as damages as it does not involve a liability of the payer. According to the decision, the Venice Municipality was aware, in entering into the Swaps, that the Banks would have hedged their financial position by back-to-back transactions with other banks.

As it was put by Mr Justice Foxton: “413. I can find nothing in that summary which would deny the Banks a change of position case where they had entered into back-to-back transactions by which they assumed (conditional) payment obligations in anticipatory reliance of receiving essentially the same payments from Venice. Indeed, the routine and objectively foreseeable nature of that anticipatory reliance, and its "back-to-back" nature (with the Banks' anticipatory reliance essentially mirroring the anticipated receipts) would seem to make this a paradigm case for the availability of the defence of change of position”.

In other word, it constituted an “anticipatory reliance” of the Banks, pushing them to buy a coverage by means of back-to-back derivatives (again, IRS) entered into with Banca IMI S.p.A and Barclays Capital (§64).

Indeed, looking carefully at the Italian Contract law is it possible to find a rule in which anticipatory reliance is considered and protected in the same way the COPD supports the payee in our case.

Art. 1328 ICC – pertaining to the conclusion of the agreement by offer and acceptance – deals with the legitimate withdrawal of the offer by the offeror, in such a way impeding the conclusion of a binding agreement.

According to the mail box rule, the standard rule also in North American Common Law<sup>13</sup>, under the Italian Civil Code, “the contract is concluded at the

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<sup>13</sup> The mailbox rule (also called the posting rule), which is the default rule, in common law, under the contract law (regarding bilateral contracts) for determining the time at which an offer is accepted, states that an offer is considered accepted at the time that the acceptance is communicated (whether by mail e-mail, etc). The main exception to the

moment that the offeror becomes aware that the offeree has accepted the offer (Art. 1326 civil code). It is, however, presumed that the offeror had such notice at the moment that the communication reached his address (Art 1335 civil code)".<sup>14</sup>

Such a rule, on one side, gives room to an (early) performance of the contract by the offeree once he has posted or issued the acceptance and prior to the arrival of it with the offeror, which would be the very moment of conclusion of the contract; on the other side, it allows the offeror to withdraw its offer prior to it becoming binding, and the agreement had arisen: indeed, according to art. 1328, first subparagraph, titled "Revocation of offer and acceptance": "An offer can be revoked until the contract is concluded".

In that case, the acceptor could have already incurred expenses and obligations (with third parties) in order to perform a contract, whose conclusion is impeded by the (although) legitimate revocation of the offer.

The rule for this occurrence is provided by the last sentence of the first subparagraph of art. 1328, which reads: "However, if the acceptor has begun performance in good faith before having notice of the revocation, the offeror is bound to indemnify him for the expenses and losses sustained in beginning performance of the contract".

The wording of the rule is significant: it does not read "recover damages" – which in Italian Contract Law is linked to a liability for breach a contract or for tort – but "indemnify", which is relief granted whereas there is no liability of the party bound for it, but the counterparty can characterize his position as a legitimate reliance.

The similarity of the two cases seems evident: by art. 1328 ICC a remedy is granted to the party which has trusted in the very likely conclusion of the contract – that failed to happen due to the legitimate revocation of the offer; in the case decided by the High Court, the Banks have trusted on the validity of the contract, which was supposed by both the parties (Venice Municipality and the Banks) until the Cattolica decision occurred as a "Fundamental Restatement" of the Italian Contract Law. Therefore, art. 1328 ICC appears applicable even reasoning a fortiori, because in the High Court case a contract did exist at the time of the incurred expenses and was not only forecasted and predicted (as assumed by art. 1328 ICC).

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rule is recognized for option contracts, as considered in the *Restatement (Second) of Contracts* §63 (1981) which reads: "Unless the offer provides otherwise, (a) an acceptance made in a manner and by a medium invited by an offer is operative and completes the manifestation of mutual assent as soon as put out of the offeree's possession, without regard to whether it ever reaches the offeror; but (b) an acceptance under an option contract is not operative until received by the offeror".

<sup>14</sup> G. ALPA – V. ZENO-ZENCOVICH, *Italian Private Law*, University of Texas and Austin Studies in Foreign and Transnational Law, New York, 2007, p. 215.

Therefore, the obiter dictum that (§393) “It is common ground that no change of position defence arises as a matter of Italian law” is worthy of a deeper consideration and cannot be accepted as a definitive statement.

## 6. The peculiarities of the COPD shaped by the High Court

Having thus set forth the points of convergence between COPD and the relief potentially granted under Italian Contract Law in similar cases, it may be of interest to highlight some peculiarities of the COPD as shaped in the decision of the High Court, as it appears as an evolution (if not an improvement) of the original common law position on the defence.

Under common law COPD, the defence is typically available to one who receives an asset, the simple example being money, in the expectation that they are not obliged to give anything in return and then makes a decision to make an unusual expenditure in an irretrievable fashion. In such circumstances, requiring the recipient to make restitution will cause injury to the recipient. The point of the COPD is to impose the loss caused on the mistaken payer whose mistake placed the recipient in this difficulty. There is no requirement that the recipient’s change of position should be foreseeable in some sense by the mistaken payer. The new version of COPD developed in *Intesa*, however, permits the defence to be raised with respect to assets transferred under a void transaction where there is no expectation by the recipient that the benefit has been transferred gratuitously in the sense that nothing must be provided in return. As we have seen, the most obvious application of this new doctrine, as in *FSM*, is with respect to expenses incurred that are necessary to the performance of the contractual obligations of the party who has received the benefit. The test articulated in *Intesa*, however, appears to be crafted more broadly to capture any case where the irretrievable use of the benefit by the recipient is “reasonably foreseeable” and not “wholly unrelated” to performance.

This new version of the COPD appears to be capable of broad application in the context of benefits transferred under void transactions. It is difficult to predict whether such a broad version of the defence will be upheld and applied in the future. If it survives appellate scrutiny, however, its ramifications would be significant.

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