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# CORPORATE & COMMERCIAL ALERT

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### The validity of market flex provisions revisited

A market flex clause is designed to provide funders with the flexibility to change the pricing and/or the structure of a financing package if there is a change in market conditions. The global COVID-19 crisis has brought about economic uncertainty and market volatility – increasing the popularity of market flex clauses amongst funders. In this article, we revisit some key legal principles underpinning the validity and enforceability of market flex clauses.

## The validity of market flex provisions revisited

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**A market flex clause is designed to provide funders with the flexibility to change the pricing and/or the structure of a financing package if there is a change in market conditions. The global COVID-19 crisis has brought about economic uncertainty and market volatility – increasing the popularity of market flex clauses amongst funders. In this article, we revisit some key legal principles underpinning the validity and enforceability of market flex clauses.**

It is customary in mortgage bonds to include a term to the effect that the mortgagee be allowed vary the interest rate unilaterally. The validity of such clause has often been attacked on the grounds that it confers upon the mortgagee an unfettered discretion and that a term of a contract leaving it to the will of one of the parties to determine the extent of his or the other party's required performance is void for vagueness. Conflicting court decisions ensued as funders tried to enforce such contracts.

After reviewing the validity of unilaterally fixing contractual terms, the Supreme Court of Appeal in *NBS Boland Bank Ltd v One Berg River Drive CC* finally settled the debate and held that, in the absence of express wording to the contrary, a clause permitting a mortgagee to vary the interest rate did not confer an unfettered discretionary power but was subject to

the inherent limitation that such power must be exercised *'arbitrio boni viri'* - which may be equated with the standard of reasonableness and honesty. Although not passing judgement on the point, the court *in obiter* expressed the view that it was yet to be seen whether a stipulation which explicitly conferred an absolute unfettered discretion upon one party to fix a performance may possibly be in conflict with public policy.

If the *NBS Boland* judgement were to be applied in the context of market flex clauses, we suggest that including wording to the effect that the market flex clause may be exercised by the funder in "*its sole and absolute discretion*" may potentially expose such clause to being challenged on the grounds of conflicting public policy. However, in the absence of explicit wording to the effect that the funder's powers are entirely unfettered, such powers are inherently subject to the limitation of reasonableness and thus valid and enforceable.

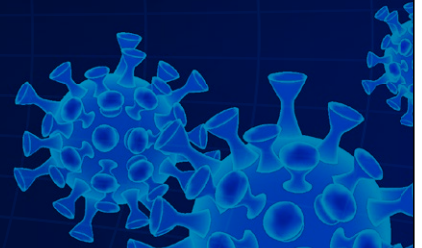
The global COVID-19 crisis has seen the emergence of strongly worded market flex clauses up for negotiation. In these market conditions it is particularly important to ensure that the wording of such clauses does not inadvertently compromise its validity but instead affords the valuable protection it is intended to provide.

*Jess Reid*

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